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# FEDERAL REGISTER

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Washington, Tuesday, March 13, 1951

## TITLE 3—THE PRESIDENT

### EXECUTIVE ORDER 10222

PROVIDING FOR CERTAIN TRANSFERS TO THE FEDERAL CIVIL DEFENSE ADMINISTRATION

By virtue of the authority vested in me by section 404 of the Federal Civil Defense Act of 1950 (Public Law 920, 81st Congress), and as President of the United States, it is ordered as follows:

1. So much of the health services and special weapons defense functions now being performed by the Health Resources Office of the National Security Resources Board as relates to civil defense is hereby transferred to the Federal Civil Defense Administration and shall remain under the jurisdiction of the Federal Civil Defense Administrator until further order of the President.

2. There shall be transferred to the Federal Civil Defense Administration such of the property and records of the National Security Resources Board as relate, as determined jointly by the Chairman of the National Security Resources Board and the Federal Civil Defense Administrator, to the functions transferred by the provisions of paragraph 1 of this order or to other functions now vested in the Federal Civil Defense Administration, and such of the personnel of the Health Resources Office of the National Security Resources Board as the said Chairman and Administrator shall jointly determine to be engaged primarily in the performance of the said transferred functions.

3. This order shall be effective as of March 4, 1951.

HARRY S. TRUMAN

THE WHITE HOUSE,
*March 8, 1951.*

[F. R. Doc. 51-3327; Filed, Mar. 12, 1951; 10:41 a. m.]

### EXECUTIVE ORDER 10223

FURTHER PROVIDING FOR THE PERFORMANCE OF CERTAIN FUNCTIONS UNDER THE DEFENSE PRODUCTION ACT OF 1950

By virtue of the authority vested in me by the Constitution and statutes, including the Defense Production Act of 1950, and as President of the United States and Commander in Chief of the armed forces, the Atomic Energy Commission is hereby designated as an additional guaranteeing agency under section 301 of the Defense Production Act of 1950, and the provisions of sections 301, 302, and 902 of Executive Order No. 10161 of September 9, 1950, as amended, together with the provisions of Executive Order No. 10182 of November 21, 1950, as amended, are hereby made applicable to the Atomic Energy Commission to the same extent as they are applicable to other guaranteeing agencies under section 301 of the Defense Production Act of 1950.

Nothing in this Executive order shall be deemed to supersede any provision of Executive Order No. 10193 of December 16, 1950.

HARRY S. TRUMAN

THE WHITE HOUSE,
*March 10, 1951.*

[F. R. Doc. 51-3330; Filed, Mar. 12, 1951; 11:28 a. m.]

## TITLE 26—INTERNAL REVENUE

### Chapter I—Bureau of Internal Revenue, Department of the Treasury

#### Subchapter A—Income and Excess Profits Taxes

[Regulations 130]

PART 40—EXCESS PROFITS TAX; TAXABLE YEARS ENDING AFTER JUNE 30, 1950

Sec.

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### THE PRESIDENT



### EXECUTIVE AGENCIES

FEDERAL REGISTER

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## CODIFICATION GUIDE

A numerical list of the parts of the Code of Federal Regulations affected by documents published in this issue. Proposed rules, as opposed to final actions, are identified as such.

## CODIFICATION GUIDE—Con.





AUTHORITY: §§ 40.0 to 40.472–8 issued under 53 Stat. 32, 467; 26 U. S. C. 62, 3791.

NOTE: *Arrangement and numbering.* Each section of the regulations has been given a key number corresponding to the number of the section or subsection of the Internal Revenue Code which the regulations section interprets. Inasmuch as the regulations constitute Part 40 of Title 26 of the Code of Federal Regulations, each key number is preceded by the number 40 and a decimal point. The key number is followed by a dash (–) and the identifying number of the regulations section.

### PART I—RATE AND COMPUTATION OF TAX

SEC. 101. IMPOSITION OF EXCESS PROFITS TAX [EXCESS PROFITS TAX ACT OF 1950, APPROVED JANUARY 3, 1951].

Effective with respect to taxable years ending after June 30, 1950, chapter 1 of the Internal Revenue Code is hereby amended by adding after section 424 the following new subchapter:

§ 40.0 *Scope of regulations in this part.* (a) The regulations in this part deal with the excess profits tax imposed by the Excess Profits Tax Act of 1950 (subchapter D of chapter 1 of the Internal Revenue Code), which act is referred to in the regulations in this part as the "act," and which tax is referred to in these regulations as the "excess profits tax." Such tax is to be distinguished from the excess profits tax imposed by subchapter E of chapter 2 of the Internal Revenue Code for taxable years beginning after December 31, 1939, and before January 1, 1946.

(b) The regulations in this part, authorized by section 62 of the Internal Revenue Code, are prescribed as a supplement to the income tax regulations applicable generally under the Internal Revenue Code. See Part 29 of this chapter (Regulations 111), applicable to income tax for taxable years beginning after December 31, 1941. The excess profits tax is imposed as a part of the

income tax on corporations under chapter 1 of the Internal Revenue Code, similar to the normal tax and surtax. The normal tax, surtax, and excess profits tax on corporations are reported on the corporation income tax return, and are treated as one tax for all purposes, including assessment, collection, payment, period of limitations, and the consolidated return privilege. See Part 29 of this chapter (Regulations 111) as to the time for filing the return and the payment of tax.

(c) The terms used in the regulations in this part in respect of the excess profits tax have, unless otherwise provided, the same meaning as when used in respect of the income tax in Part 29 of this chapter (Regulations 111). Similarly, all provisions of law (including penalties) applicable in respect of the income tax under Part 29 of this chapter (Regulations 111), are, insofar as not inconsistent with the regulations in this part, applicable in respect of the excess profits tax. Every corporation (except a corporation exempt from excess profits tax under section 454) must file with, and as a part of, its income tax return the applicable schedule with respect to the excess profits tax.

(d) Each section, subsection, or paragraph of the Internal Revenue Code set forth in this part shall be considered as a part of the respective regulations section to which it corresponds.

(e) Except as otherwise indicated, the statutory references in the regulations in this part are to the Internal Revenue Code. As used in the regulations in this part, the word "Code" means the Internal Revenue Code.

SEC. 430. IMPOSITION OF TAX.

(a) *General rule.* In addition to other taxes imposed by this chapter, there shall be levied, collected, and paid for each taxable year ending after June 30, 1950, and beginning before July 1, 1953, upon the adjusted excess profits net income, as defined in section 431, of every corporation (except a corporation exempt under section 454) an excess profits tax equal to whichever of the following amounts is the lesser:

(1) 30 per centum of the adjusted excess profits net income, or

(2) An amount equal to the excess of 62 per centum of the excess profits net income for the taxable year over the tax which would be imposed for the taxable year under sections 13, 14, and 15, supplement G, and supplement Q, whichever are applicable to the taxpayer, computed (subject to section 108 and section 141, if applicable) as if the amount of the normal-tax net income and the amount of the corporation surtax net income (or the amount subject to the rate of tax in such supplement) were equal to the amount of the excess profits net income for such year.

(b) *Taxable years beginning before July 1, 1950, and ending after June 30, 1950.* In the case of a taxable year beginning before July 1, 1950, and ending after June 30, 1950, the tax imposed by subsection (a) shall be an amount equal to that portion of a tentative tax, determined under subsection (a), which the number of days in such taxable year after June 30, 1950, bears to the total number of days in such taxable year.

(c) *Taxable years beginning before July 1, 1953, and ending after June 30, 1953.* In the case of a taxable year beginning before July 1, 1953, and ending after June 30, 1953, the tax imposed by subsection (a) shall be an amount equal to that portion of a tentative tax, determined under subsection (a), which the number of days in such taxable year before July 1, 1953, bears to the total number of days in such taxable year.

(d) *Mutual insurance companies.* In the case of a mutual insurance company other than life or marine, if the gross amount received from interest, dividends, rents, and premiums (including deposits and assessments) is over $75,000 but less than $125,000, the tax imposed under this section shall be an amount which bears the same proportion to the amount ascertained under this section, computed without reference to this subsection, as the excess over $75,000 of such gross amount received bears to $50,000.

(e) *Cross references.* For special rules for computation of the tax imposed by subsection (a) in the case of—

(1) Short taxable years, see section 433 (a) (2);

(2) Corporations engaged in mining of strategic materials, see section 450 (a);

(3) Abnormalities in income in taxable period, see section 456;

(4) Corporations completing contracts under Merchant Marine Act, see section 457.

§ 40.430–1 *Scope of tax.* The excess profits tax is imposed by subchapter D of chapter 1 of the Internal Revenue Code and is in addition to all other taxes imposed by chapter 1. The excess profits tax is imposed upon the adjusted excess profits net income of every corporation, both domestic and foreign, for each taxable year ending after June 30, 1950, and beginning before July 1, 1953, except in the case of certain corporations which are exempt from the tax under the provisions of section 454. A personal service corporation, as defined in section 449, may, if it is not a member of an affiliated group of corporations filing consolidated returns under section 141, elect not to be subject to the excess profits tax, thereby making its income taxable to its shareholders as provided in Supplement S of the Internal Revenue Code. See section 449.

§ 40.430–2 *Rate of tax*—(a) *In general.* (1) The excess profits tax shall be whichever of the following is the lesser:

(i) An amount equal to 30 percent of the adjusted excess profits net income, or

(ii) An amount equal to the excess of 62 percent of the excess profits net income for the taxable year over the tax which would be imposed for such year under sections 13, 14, and 15, Supplement G, and Supplement Q, whichever are applicable to the taxpayer, computed (subject to section 108, relating to fiscal year taxpayers, and section 141, relating to consolidated returns, if applicable) as if the amount of the normal-tax net income and the amount of the corporation surtax net income (or the amount subject to the rate of tax in such supplement) were equal to the amount of the excess profits net income for such year.

(2) For purposes of section 430 (a) (2) and of subdivision (ii) of subparagraph (1) of this paragraph, the tax which would be imposed under sections 13, 14, and 15, Supplement G, and Supplement Q shall be determined without regard to the credit under section 131 for taxes paid to a foreign country or a possession of the United States. In the case of the calendar year 1950, the tax which would be imposed under section 15 shall be determined without regard to any reduction by reference to the credit provided in section 26 (a), relating to credit for interest on obligations of the United States and its instrumentalities, and therefore shall be equal to the tentative surtax which would be imposed under section 15. Thus, in the case of a taxpayer other than an insurance company or a regulated investment company subject to Supplement G or Supplement Q, the normal tax referred to in section 430 (a) (2) for the calendar year 1950 is 23 percent of the excess profits net income, and the surtax referred to in section 430 (a) (2) for the calendar year 1950 is 19 percent of the amount by which the excess profits net income exceeds $25,000, plus, if a consolidated return is filed, 2 percent of the excess profits net income.

(b) *Taxable years beginning before July 1, 1950, and ending after June 30, 1950.* In the case of any taxable year which begins before July 1, 1950, and ends after June 30, 1950 (including the calendar year 1950), the excess profits tax will be an amount which is proportionate to the part of the year falling after June 30, 1950. The tax will be an amount which is equal to that portion of a tentative tax computed under section 430 (a) and under paragraph (a) of this section as the number of days in the taxable year after June 30, 1950, bears to the total number of days in such year. Thus, in the case of the calendar year 1950, the tax will be 184/365ths of the tentative tax determined under paragraph (a) of this section.

(c) *Taxable years beginning before July 1, 1953, and ending after June 30, 1953.* In the case of a taxable year which begins before July 1, 1953, and ends after June 30, 1953, the excess profits tax will be an amount equal to that portion of a tentative tax determined under section 430 (a) and under paragraph (a) of this section as the number of days in such year prior to July 1, 1953, bears to the total number of days in such year.

(d) *Mutual insurance companies.* If a mutual insurance company, other than life or marine, receives a gross amount from interest, dividends, rents, and premiums (including deposits and assessments) in excess of $75,000 but less than $125,000, the tax imposed under section 430 is an amount which bears the same proportion to the amount of tax otherwise determined under such section, computed without regard to section 430 (d) and the provisions of this paragraph, as the excess over $75,000 of such gross amount received bears to $50,000. For example, assume that a mutual insurance company (other than a life or marine insurance company) receives a gross amount from interest, dividends, rents, and premiums of $115,000, and that its excess profits tax computed under section 430 (a) is $18,000. Under section 430 (d), the excess profits tax imposed under section 430 is $14,400, that is, $\left(\frac{\$115,000-\$75,000}{\$50,000}\right)\times\$18,000$.

(e) *Cross references.* As to the exemption of income in the case of certain corporations engaged in mining strategic minerals, see section 450; as to the excess profits tax in the case of corporations completing contracts under the Merchant Marine Act, see section 457; and in the case of corporations deriving abnormal income in the taxable year, see section 456. For the computation of the excess profits tax for a taxable year of less than 12 months, see the provisions of section 433 (a) (2).

SEC. 431. DEFINITION OF ADJUSTED EXCESS PROFITS NET INCOME.

The term "adjusted excess profits net income" in the case of any taxable year means the excess profits net income (as defined in section 433 (a)) minus the sum of:

(1) *Excess profits credit.* The amount of the excess profits credit allowed under section 434; and

(2) *Unused excess profits credits.* The amount of the unused excess profits credit adjustment for the taxable year computed in accordance with section 432.

If such sum is less than $25,000, it shall be increased to $25,000.

§ 40.431–1 *Definition of adjusted excess profits net income.* Adjusted excess profits net income in the case of any taxable year is excess profits net income, as defined in section 433 (a), minus the sum of (a) the taxpayer's excess profits credit allowed under section 434 and (b) its unused excess profits credit adjustment computed in accordance with section 432. If the sum of the excess profits credit and the unused excess profits credit adjustment is less than $25,000, such sum shall be increased to $25,000.

SEC. 432. UNUSED EXCESS PROFITS CREDIT ADJUSTMENT.

(a) *Computation of unused excess profits credit adjustment.* The unused excess profits credit adjustment for any taxable year shall be the aggregate of the unused excess profits credit carry-overs and unused excess profits credit carry-back to such taxable year.

(b) *Definition of unused excess profits credit.* The term "unused excess profits credit" means the excess, if any, of the excess profits credit for any taxable year ending after June 30, 1950, and beginning before July 1, 1953, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year, and computed without the allowance of any deduction under section 23 (s) (relating to net operating losses). The unused excess profits credit for a taxable year of less than 12 months shall be an amount which is such part of the unused excess profits credit determined under the preceding sentence as the number of days in the taxable year is of the number of days in the 12 months ending with the close of the taxable year. The unused excess profits credit for a taxable year beginning before July 1, 1950, and ending after June 30, 1950, shall be an amount which is such part of the unused excess profits credit determined under the preceding provisions of this subsection as the number of days in such taxable year after June 30, 1950, is of the total number of days in such taxable year. The unused excess profits credit for a taxable year beginning before July 1, 1953, and ending after June 30, 1953, shall be an amount which is such part of the unused excess profits credit determined under the preceding provisions of this subsection as the number of days in such taxable year before July 1, 1953, is of the total number of days in such taxable year. There shall be no unused excess profits credit for any taxable year for which the taxpayer is exempt from taxation under this subchapter.

(c) *Amount of carry-back and carry-over—*

(1) *Unused excess profits credit carry-back.* If for any taxable year beginning after July 1, 1950, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-back for the preceding taxable year.

(2) *Unused excess profits credit carry-over.* If for any taxable year ending after June 30, 1950, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-over for each of the five succeeding taxable years, except that the carry-over in the case of each such succeeding taxable year (other than the first succeeding taxable year) shall be the excess, if any, of the amount of such unused excess profits credit over the sum of the adjusted excess profits net income for each of the intervening taxable years computed—

(A) By determining the unused excess profits credit adjustment for each intervening taxable year without regard to such unused excess profits credit or to any unused excess profits credit for any succeeding year, and

(B) Without regard to the last sentence of section 431.

For the purpose of the preceding sentence the unused excess profits credit for any taxable year beginning after July 1, 1950, shall first be reduced by the amount, if any, of the adjusted excess profits net income for the preceding taxable year computed—

(C) By determining the unused excess profits credit adjustment for such preceding taxable year without regard to such unused excess profits credit, and

(D) Without regard to the last sentence of section 431.

If such preceding taxable year began prior to July 1, 1950, the reduction referred to in the preceding sentence shall be an amount which is such part of the reduction determined under the preceding sentence, or such part of the unused excess profits carry-back for such preceding taxable year, whichever is the lesser, as the number of days in such taxable year after June 30, 1950, is of the total number of days in such preceding taxable year.

(d) *No carry-back to taxable years ending prior to July 1, 1950.* As used in this section the term "preceding taxable year" does not include any taxable year ending prior to July 1, 1950.

(e) *Unused excess profits credit of year of liquidation.* For any taxable year during which the taxpayer (1) completes the distribution of substantially all of its assets in liquidation, or (2) completes the conversion of substantially all of its assets into assets not held in good faith for the purposes of the business, then the unused excess profits credit for such year shall be an amount which is such part of the unused excess profits credit determined under the preceding provisions of this section as the number of days in the taxable year prior to the date of the completion (described in (1) or (2), whichever is earlier) is of the total number of days in the taxable year, and no part of the unused excess profits credit for such year shall be an unused excess profits credit carry-over for any succeeding taxable year.

§ 40.432–1 *Unused excess profits credit adjustment*—(a) *Unused excess profits credit.* Section 432 provides that the unused excess profits credit for any taxable year ending after June 30, 1950, and beginning before July 1, 1953, is the excess of the corporation's excess profits credit for such taxable year over its excess profits net income for such year computed without regard to the net operating loss deduction and computed on the basis of the excess profits credit applicable to such year. If the taxable year is less than 12 months the unused excess profits credit will be that portion of the unused excess profits credit determined under the general rule as the number of days in the taxable year is of the number of days in the 12-month period ending with the close of the taxable year. If the taxable year began before July 1, 1950, and ends after June 30, 1950, the unused excess profits credit will be an amount which is such portion of the unused excess profits credit determined under the general rule as the number of days in the taxable year after June 30, 1950, is of the total number of days in such taxable year. If the taxable year begins before July 1, 1953, and ends after June 30, 1953, the unused excess profits credit will be an amount which is such portion of the unused excess profits credit determined under the general rule as the number of days in the taxable year before July 1, 1953, is of the total number of days in such taxable year. There shall be no unused excess profits credit for any taxable year for which the taxpayer is exempt under section 454.

(b) *Unused excess profits credit carry-back and carry-over.* (1) The unused excess profits credit determined under section 432 (b) and under paragraph (a) of this section for any taxable year ending after June 30, 1950, will first be carried back to the first preceding taxable year as an unused excess profits credit carry-back. The balance of the unused credit may then be carried over to the five succeeding taxable years as an unused excess profits credit carry-over. If the preceding taxable year ends after June 30, 1950, the unused excess profits credit carry-over to the first succeeding taxable year will be the excess of the unused credit over the adjusted excess profits net income of the preceding taxable year. The adjusted excess profits net income for such preceding taxable year will be determined by computing the unused excess profits credit adjustment for such preceding taxable year without regard to the unused credit carry-back and without regard to the last sentence of section 431 providing for a minimum excess profits credit plus unused excess profits credit adjustment of $25,000.

(2) If the preceding taxable year began prior to July 1, 1950, the amount by which the unused credit is reduced for the purpose of computing the carry-over is an amount which is such part of the reduction determined under subparagraph (1) of this paragraph, or such part of the unused excess profits credit carry-back for such preceding taxable year, whichever is the lesser, as the number of days in such preceding taxable year after June 30, 1950, is of the total number of days in such preceding taxable year.

(3) In determining the unused excess profits credit carry-over to the second, third, fourth, and fifth taxable years, the unused excess profits credit is further reduced by the adjusted excess profits net income for each of the intervening tax-

able years. For such purpose, the adjusted excess profits net income for any intervening taxable year is determined (i) by computing the unused excess profits credit adjustment for such intervening year without regard to such unused credit and without regard to any unused excess profits credit for any year subsequent to the year of such unused credit, and (ii) by disregarding the last sentence of section 431 providing for a minimum excess profits credit plus unused excess profits credit adjustment of $25,000.

(4) For the purpose of computing the unused excess profits credit carry-over, an unused excess profits credit will not be decreased by reference to any taxable year ending prior to July 1, 1950. No unused excess profits credit carry-back to, and no unused excess profits credit carry-over from, any taxable year ended prior to July 1, 1950, is allowed.

(c) *Unused excess profits credit of year of liquidation.* If the taxpayer has distributed substantially all its assets in liquidation, or has converted substantially all its assets into assets not held in good faith for purposes of the business, see section 432 (e).

(d) *Two or more prorations of unused credit.* In any case in which the general rule stated in the first sentence of paragraph (a) of this section is subject to more than one of the special rules in paragraphs (a) and (c) of this section relating to proration of the unused excess profits credit, the special rules shall be applied in the order in which set forth in this section.

SEC. 433. EXCESS PROFITS NET INCOME.

(a) *Taxable years ending after June 30, 1950.* The excess profits net income for any taxable year ending after June 30, 1950, shall be the normal-tax net income, as defined in section 13 (a) (2), for such year increased or decreased by the following adjustments:

(1) *Adjustments*—(A) *Dividends received.* The credit for dividends received shall apply, without limitation (except the limitation relating to dividends in kind), to all dividends on stock of all corporations, except that no credit for dividends received shall be allowed with respect to dividends (actual or constructive) on stock of foreign personal holding companies or dividends on stock which is not a capital asset;

(B) *Disallowance of certain credits.* In computing such normal-tax net income the credits provided in section 26 (h) and (i) shall not be allowed;

(C) *Gains and losses from sales or exchanges of capital assets.* There shall be excluded gains and losses from sales or exchanges of capital assets;

(D) *Income from retirement or discharge of bonds, and so forth.* There shall be excluded, in the case of any taxpayer, income derived from the retirement or discharge by the taxpayer of any bond, debenture, note, or certificate or other evidence of indebtedness, if the obligation of the taxpayer has been outstanding for more than 6 months, including, in case the issuance was at a premium, the amount includible in income for such year solely because of such retirement or discharge;

(E) *Refunds and interest on Agricultural Adjustment Act taxes.* There shall be excluded income attributable to refund of tax paid under the Agricultural Adjustment Act of 1933, as amended, and interest upon any such refund;

(F) *Deductions on account of retirement or discharge of bonds, and so forth.* If during the taxable year the taxpayer retires or discharges any bond, debenture, note, or certificate or other evidence of indebtedness, if the obligation of the taxpayer has been outstanding for more than 6 months, the following deductions for such taxable year shall not be allowed:

(i) The deduction allowable under section 23 (a) for expenses paid or incurred in connection with such retirement or discharge;

(ii) The deduction for losses allowable by reason of such retirement or discharge; and

(iii) In case the issuance was at a discount, the amount deductible for such year solely because of such retirement or discharge;

(G) *Recoveries of bad debts.* There shall be excluded income attributable to the recovery of a bad debt if the deduction of such debt was allowable from gross income for any taxable year beginning before January 1, 1940, or beginning after December 31, 1945, and ending before July 1, 1950, or if such debt was properly charged to a reserve for bad debts during any such taxable year;

(H) *Life insurance companies.* In the case of a life insurance company, there shall be deducted from the normal tax net income the excess of (1) the product of (i) the figure determined and proclaimed under section 202 (b) and (ii) the excess profits net income computed without regard to this subparagraph, over (2) the adjustment for certain reserves provided in section 202 (c). If the excess profits credit for the taxable year is computed under section 436, there shall be deducted from the normal tax net income only 50 per centum of the amount determined under the preceding sentence;

(I) *Nontaxable income of certain industries with depletable resources.* In the case of a producer of minerals, or a producer of logs or lumber from a timber block, or a lessor of mineral property, or a timber block, as defined in section 453, there shall be excluded nontaxable income from exempt excess output of mines and timber blocks provided in section 453; in the case of a natural gas company, as defined in section 453, there shall be excluded nontaxable income from exempt excess output provided in section 453; and in the case of a producer of minerals, or a producer of logs or lumber from a timber block, there shall be excluded nontaxable bonus income provided in section 453. In respect of nontaxable bonus income provided in section 453 (c), a corporation described in section 453 (c) (2) shall be deemed a producer of minerals for the purposes of this subparagraph;

(J) *Net operating loss deduction adjustment.* The net operating loss deduction shall be adjusted as follows:

(i) In computing the net operating loss for any taxable year under section 122 (a), and the net income for any taxable year under section 122 (b), the deduction for interest shall be reduced by the amount of any reduction under subparagraph (N) or (O), whichever is applicable upon the basis of the excess profits credit for such taxable year; and

(ii) In lieu of the reduction provided in section 122 (c), such reduction shall be in the amount by which the excess profits net income computed with the exceptions and limitations specified in section 122 (d) (1), (2), (3), and (4), and computed without regard to subparagraph (C), without regard to any credit for dividends received, and without regard to any credit for interest received provided in section 26 (a) exceeds the excess profits net income (computed without the net operating loss deduction); and

(iii) If the excess profits credit for the first taxable year under this subchapter is computed under section 435 or is computed under section 436 (a) by use of the historical invested capital determined under section 458, the taxpayer may elect in its return for such taxable year to compute its net operating loss deduction for the purposes of this subsection for all taxable years by treating an amount equal to the base period loss adjustment (as defined in clause (iv)) as a net operating loss carry-over from the last taxable year ending before July 1, 1950, but for such purposes the net income computed under section 122 (b) for any taxable year ending before July 1, 1950, shall be determined without regard to such carry-over;

(iv) For the purposes of clause (iii), the base period loss adjustment shall be the amount of the recent loss adjustment determined under section 437 (f), using the base period as the recent loss period, and computed by limiting the amount of the net operating loss for any taxable year beginning before January 1, 1948, to an amount equal to the net operating loss carry-over from such taxable year to the taxable year immediately succeeding such taxable year; and

(v) If the taxpayer makes the election provided in clause (iii) of this subparagraph, the net operating loss deduction for the purposes of this subsection for each taxable year ending after June 30, 1950 (whether or not the credit for such taxable year is computed under section 435) shall be computed without regard to the net operating loss for any taxable year ending before July 1, 1950, and the net operating loss carry-over specified in clause (iii) of this subparagraph shall not be allowed as a net operating loss carry-over to any taxable year for which the excess profits credit is not computed under section 435 and is not computed under section 436 (a) by use of the historical invested capital determined under section 458;

(K) *Taxes paid by lessee.* If under a lease for a term of more than 20 years entered into prior to December 1, 1950, the lessee is obligated to pay any portion of the tax imposed by this chapter upon the lessor with respect to the rentals derived by such lessor from such lessee, or is obligated to reimburse the lessor for any portion of the tax imposed by this chapter upon the lessor with respect to the rentals derived by such lessor from such lessee, such payment or reimbursement of the tax imposed by this chapter shall be excluded by the lessor and a deduction therefor shall not be allowed to the lessee. For the purposes of this subparagraph an agreement for lease of railroad properties entered into prior to December 1, 1950, shall be considered to be a lease including such term as the total number of years such agreement may, unless sooner terminated, be renewed or continued under the terms of the agreement, and any such renewal or continuance under such agreement shall be considered part of the lease entered into prior to December 1, 1950;

(L) *Bad debts in case of banks.* In the case of a bank (as defined in section 104) using the reserve method of accounting for bad debts, there shall be allowed, in lieu of the amount allowable under the reserve method for bad debts, a deduction for debts which became worthless within the taxable year, in whole or in part, within the meaning of section 23 (k);

(M) *Blocked foreign income.* There shall be excluded income derived from sources within any foreign country to the extent that such income would, but for monetary, exchange, or other restrictions imposed by such foreign country, have been includible in the gross income of the taxpayer for any taxable year which preceded its first taxable year under this subchapter. In determining the taxable year for which income derived from foreign sources would have been includible (but for such restrictions) in cases where specific identification cannot be made, such determinations shall be made in accordance with regulations prescribed by the Secretary. Where income derived from sources within any foreign country is includible (without regard to this sentence) in a taxable year succeeding the first taxable year under this subchapter, and but for monetary, exchange, or other restrictions imposed by such foreign country would have

been includible in the gross income of the taxpayer for its first taxable year under this subchapter, such income, in case such first taxable year began before July 1, 1950, shall be considered (in the application of this subparagraph) as having been includible in gross income of a taxable year which preceded such first taxable year in an amount equal to that portion of such income as the number of days prior to July 1, 1950, in such first taxable year bears to the total number of days in such first taxable year. Deductions properly chargeable and allocable to income excluded under this subparagraph shall not be allowed:

(N) *Interest—credit based upon invested capital.* If the excess profits credit for the taxable year is computed under section 436 the deduction for interest shall be reduced by an amount equal to 75 per centum of so much of such interest as represents interest on the indebtedness included in the daily amounts of borrowed capital (determined under section 439 (b)).

(O) *Interest—credit based upon income.* If the excess profits credit for the taxable year is computed under section 435, the deduction for interest shall be reduced by an amount which bears the same ratio to the interest on the indebtedness included in the daily amounts of borrowed capital (determined under section 439 (b)) as the excess of the amount determined under section 435 (g) (3) (C) over the aggregate, divided by the number of days in the taxable year, of the amount determined under section 435 (g) (4) (E) for each day of the taxable year, bears to the average borrowed capital for the taxable year (as defined in section 439 (a)).

(P) *Payments to encourage exploration, development, and mining for defense purposes.* An amount paid to a taxpayer by the United States (or any agency or instrumentality thereof), whether by grant or loan, and whether or not repayable, for the encouragement of exploration, development or mining of critical and strategic minerals or metals pursuant to or in connection with any undertaking approved by the United States (or any of its agencies or instrumentalities) and for which an accounting is made or required to be made to an appropriate governmental agency, and the forgiveness or discharge of any such amount, shall be excluded in computing excess profits net income; and any expenditures (other than expenditures made after the repayment of such grant or loan) attributable to such grant or loan shall not be deductible by the taxpayer as an expense nor increase the basis of the taxpayer's property either for determining gain or loss on sale, exchange, or other disposition or for computing depletion or depreciation, but upon the repayment of any portion of any such grant or loan which has been expended in accordance with the terms thereof such deductions and such increase in basis shall to the extent of such repayment be allowed as if made at the time of such repayment;

(Q) *Income from installment sales, long-term contracts etc.* For adjustment, in the case of a taxpayer making an election provided in section 455, with respect to income derived from installment sales, installment sales obligations, or long-term contracts, see section 455.

(2) *Taxable year less than twelve months—*(A) *General rule.* If the taxable year is a period of less than twelve months the excess profits net income for such taxable year (referred to in this paragraph as the "short taxable year") shall be placed on an annual basis by multiplying the amount thereof by the number of days in the twelve months ending with the close of the short taxable year and dividing by the number of days in the short taxable year. The tax imposed by section 430 shall be such part of the tax computed on such annual basis as the number of days in the short taxable year is of the number of days in the twelve months ending with the close of the short taxable year.

(B) *Exception.* If the taxpayer establishes its adjusted excess profits net income for the period of twelve months beginning with the first day of the short taxable year, computed as if such twelve-month period were a taxable year, under the law applicable to the short taxable year, and using the credits applicable in determining the adjusted excess profits net income for such short taxable year, then the tax for the short taxable year shall be reduced to an amount which is such part of the tax computed on such adjusted excess profits net income so established as the excess profits net income for the short taxable year is of the excess profits net income for such twelve-month period. The taxpayer (other than a taxpayer to which the next sentence applies) shall compute the tax and file its return without the application of this subparagraph. If, prior to one year from the date of the beginning of the short taxable year, the taxpayer has disposed of substantially all its assets, in lieu of the twelve-month period provided in the preceding provisions of this subparagraph, the twelve-month period ending with the close of the short taxable year shall be used. For the purposes of this subparagraph, the excess profits net income for the short taxable year shall not be placed on an annual basis as provided in subparagraph (A), and the excess profits net income for the twelve-month period used shall in no case be considered less than the excess profits net income for the short taxable year. The benefits of this subparagraph shall not be allowed unless the taxpayer, at such time as regulations prescribed hereunder require, makes application therefor in accordance with such regulations, and such application, in case the return was filed without regard to this subparagraph, shall be considered a claim for credit or refund. The Secretary shall prescribe such regulations as he may deem necessary for the application of this subparagraph.

(C) *Section 47 (c) not applicable.* The provisions of section 47 (c) shall not apply to the tax imposed by this subchapter.

§ 40.433 (a)–1 *Excess profits net income for the taxable year.* The excess profits net income computed under section 433 (a) for any taxable year ending after June 30, 1950, is the normal-tax net income increased or decreased by the adjustments provided in section 433 (a) (1). The adjustment provided by section 433 (a) (1) (N) applies exclusively to the case of a taxpayer computing its excess profits credit for the taxable year upon the basis of invested capital under section 436, and the adjustment provided by section 433 (a) (1) (O) applies exclusively to the case of a taxpayer computing its excess profits credit upon the basis of income under section 435. There are also certain differences in the amount of the deduction allowed under section 433) (a) (1) (H) and certain differences in the determination of the net operating loss deduction adjustment under section 433 (a) (1) (J), dependent upon whether the excess profits credit for the taxable year is computed under the income method or under the invested capital method. In general, the other adjustments under section 433 (a) (1) are the same whether excess profits credit is computed under the income method or the invested capital method.

§ 40.433 (a)–2 *Computation of excess profits net income for the taxable year.* (a) Section 433 (a) (1) (A) provides for the allowance, in computing excess profits net income, of a credit for dividends received. The credit is allowed without limitation in the case of dividends received from both domestic and foreign corporations, except that (1) the limitation provided by section 26 (b) with respect to dividends in kind received after August 31, 1950, applies, (2) no credit is allowed with respect to dividends (actual or constructive) on stock of foreign personal holding companies, and (3) no credit is allowed with respect to dividends on stock which is not a capital asset. The credit for dividends received from certain domestic corporations provided for by section 26 (b), for normal-tax purposes, is limited generally to 85 percent of the amount received. Excess profits net income is computed by decreasing normal-tax net income by the excess of the credit computed under section 433 (a) (1) (A) over the credit allowed under section 26 (b) in computing such normal-tax net income. In the case of a dividend received in kind after August 31, 1950, the amount of the dividend for the purpose of section 433 (a) (1) (A) is deemed not to exceed the adjusted basis of the property so distributed in the hands of the distributing corporation at the time of the distribution, increased by the amount of the gain or decreased by the amount of loss recognized to the distributing corporation by reason of such distribution.

(b) Section 433 (a) (1) (B) provides for an adjustment in respect of any credit which may have been allowed under section 26 (h) (relating to the credit for dividends paid on certain preferred stock), or under section 26 (i) (relating to the credit granted Western Hemisphere Trade Corporations), in computing normal-tax net income. The effect of the adjustment is to increase normal-tax net income by the amount of any such credit or credits.

(c) Gains and losses from sales or exchanges of capital assets, whether long-term or short-term, are excluded under section 433 (a) (1) (C) in determining excess profits net income. Such gains and losses are determined under the definitions contained in, and in the manner prescribed by, section 117. Accordingly, excess profits net income is computed by decreasing normal-tax net income by the amount of the net capital gain of the corporation. Thus, if the gains of the corporation described in section 117 (j) exceed the losses described in that section, such gains and losses are considered capital gains and losses, and are included in determining net capital gain for the purpose of the adjustment required by section 433 (a) (1) (C). If the gains described in section 117 (j) do not exceed the losses described in that section, such gains and losses are not considered capital gains and losses, and are not taken into account in computing the adjustment required by section 433 (a) (1) (C). No adjustment under section 433 (a) (1) (C) is required for any net capital loss which is not allowed as a deduction in the computation of normal-tax net income.

(d) In the case of a taxpayer which retires or discharges any bond, debenture, note, or certificate or other evidence of indebtedness outstanding for

more than six months, section 433 (a) (1) (D) requires, for the purpose of computing excess profits net income, that normal tax net income be decreased by the amount of any income derived from such retirement or discharge. Similarly, section 433 (a) (1) (F) requires, for the purpose of computing excess profits net income, that normal-tax net income be increased by the amount of any deductions allowed under section 23 (a) in connection with the retirement or discharge of any such bond, etc., and by the amount of any deduction allowed for losses resulting from such retirement or discharge. In the case of the discharge or retirement of bonds which were issued at a premium, the normal-tax net income is also decreased, under section 433 (a) (1) (D) by the amount of any premium includible in income for such taxable year solely because of the retirement or discharge, but no adjustment is made for any accrued amortization of bond premium for that part of the taxable year which precedes the date of the retirement or discharge. In the case of bonds which were issued at a discount, the normal-tax net income is increased by the amount of discount which was deductible solely because of the retirement or discharge, but no adjustment is made for any accrued amortization of bond discount for that part of the taxable year which precedes the date of the retirement or discharge.

(e) As used in section 433 (a) (1) (D) and (F), the term "indebtedness" includes indebtedness assumed by the taxpayer even though such indebtedness is evidenced, so far as the taxpayer is concerned, only by a contract (which has been outstanding for more than six months) with the person whose liabilities have been assumed. Also, a renewal obligation is to be considered to be outstanding for more than six months if the original obligation and the renewal obligation taken together have been outstanding for a total of more than six months. The term "other evidence of indebtedness" does not include open account book entries.

(f) Under the adjustment provided by section 433 (a) (1) (E), normal-tax net income is decreased by the amount of any income attributable to refund of tax paid under the Agricultural Adjustment Act of 1933, as amended, and any interest upon any such refund. Such refunds include only those made under Title VII of the Revenue Act of 1936 and refunds made to processors under section 15 (a) of the Agricultural Adjustment Act as reenacted by section 601 of the Revenue Act of 1936.

(g) The provisions of section 433 (a) (1) (G) require the exclusion from excess profits net income of any income attributable to the recovery of a bad debt, if either (1) a deduction from gross income was allowable with reference to such debt for any taxable year for which an excess profits tax was not imposed (that is, a taxable year beginning before January 1, 1940, or a taxable year beginning after December 31, 1945, and ending before July 1, 1950), or (2) if such debt was properly charged to a bad debt reserve during any such taxable year. For example, if a deduction of $10,000 from gross income would have been allowable for an addition to the reserve account in the absence of bad debts recovered, which had been charged against the reserve account for the year 1948, and if no deduction is required for the taxable year by reason of such bad debts recovered in the amount of $13,000 and credited to the reserve account, the adjustment of the normal-tax net income for the taxable year under section 433 (a) (1) (G) would be limited to $10,000. In such case, the excess of the bad debt recoveries over the amount which would have been added to the reserve account had there been no such recoveries, i. e., the $3,000, will decrease the amount to be added to the reserve in the following year, and accordingly such amount may be excluded under section 433 (a) (1) (G) in such following year.

(h) In the case of a life insurance company which does not compute its excess profits credit under section 436, normal-tax net income is decreased for the purpose of computing excess profits net income by the adjustment provided in the first sentence of section 433 (a) (1) (H). The amount of such decrease is determined by multiplying the excess profits net income determined without regard to section 433 (a) (1) (H) by the figure determined and proclaimed by the Secretary of the Treasury pursuant to section 202 (b) for the taxable year, and subtracting from the product thus obtained the amount of the adjustment for certain reserves provided by section 202 (c). If the taxpayer computes its excess profits credit upon the basis of invested capital under section 436, only 50 percent of the amount determined in the manner described in the preceding sentence may be deducted from normal-tax net income in computing excess profits net income.

(i) See section 433 (a) (1) (I) for the exclusion of nontaxable income from exempt excess output of mines and timber blocks provided in section 453 in the case of a producer of minerals or a producer of logs or lumber from a timber block, or in the case of a lessor of a mineral property, a coal mining or metal mining property, or a timber block, as defined in section 453; for the exclusion of nontaxable income from exempt excess output provided in section 453 in the case of a natural gas company as defined in section 453; and for the exclusion of nontaxable bonus income provided in section 453 in the case of a producer of minerals or a producer of logs or lumber from a timber block as defined in section 453. A lessor of a mineral property, a coal or metal mining property, or a timber block is not entitled to the benefit of the exclusion for nontaxable bonus income. For the purposes of the exclusion pursuant to the provisions of section 433 (a) (1) (I) of nontaxable bonus income provided in section 453 (c), a corporation described in section 453 (c) (2) as one which extracts or recovers a mineral product from mine tailings and which owns no economic interest in the mineral property from which the ore containing such tailings was mined shall be deemed to be a producer of the minerals so extracted or recovered.

(j) (1) Section 433 (a) (1) (J) provides for recomputation of the net operating loss deduction in computing excess profits net income. The various steps in computing the deduction are to be taken in the same manner and for the same years as are provided in section 122 and in the regulations thereunder, except as otherwise prescribed in the rules set forth in section 433 (a) (1) (J). The exceptions prescribed by section 433 (a) (1) (J) require that, in the computation of the net operating loss for any taxable year under section 122 (a) and in the computation of the net income for any taxable year under section 122 (b), the deduction for interest shall be reduced by the amount of any reduction under section 433 (a) (1) (N) or (O) (relating to interest adjustment with respect to borrowed capital), depending on whether the excess profits credit for such taxable year is based upon invested capital or income, respectively. Furthermore, in lieu of the reduction prescribed in section 122 (c) for converting the aggregate of the net operating loss carry-overs and carry-backs to the taxable year into the net operating loss deduction, the reduction for such purpose shall be the amount by which the excess profits net income for the taxable year in which the deduction is allowable, computed with the exceptions and limitations specified in section 122 (d) (1), (2), (3), and (4) and computed without regard to section 433 (a) (1) (C) (relating to gains and losses from the sale or exchange of capital assets), without regard to any credit for dividends received, and without regard to any credit for interest received provided in section 26 (a) exceeds the excess profits net income for such taxable year (computed without any net operating loss deduction). The net operating loss deduction so computed with the adjustments prescribed by section 433 (a) (1) (J) is deducted to determine excess profits net income, in lieu of the net operating loss deduction otherwise prescribed in sections 23 (s) and 122.

(2) In addition to the foregoing, section 433 (a) (1) (J) provides that if the excess profits credit for the first taxable year ending after June 30, 1950, is computed under section 435 (relating to the excess profits credit based on income), or is computed under section 436 (a) by use of the historical invested capital determined under section 458, the taxpayer may elect in its return (by a statement attached thereto) for such taxable year to compute its net operating loss deduction for all taxable years, for the purpose of computing excess profits net income, by treating an amount equal to the base period loss adjustment (as defined in section 433 (a) (1) (J) (iv)) as a net operating loss carry-over from the last taxable year ending before July 1, 1950, but in such case the net income computed under section 122 (b) for any taxable year ending before July 1, 1950, shall be determined without regard to such carry-over. For the purpose of such treatment, the base period loss adjustment shall be the amount of the recent loss adjustment determined under section 437 (f) by using the base period as the recent loss period, and computed

by limiting the amount of the net operating loss for any taxable year beginning before January 1, 1948, to an amount equal to the net operating loss carry-over from such taxable year to the taxable year immediately succeeding such taxable year. If the taxpayer makes the above election, as provided for in section 433 (a) (1) (J) (iii), the net operating loss deduction for each taxable year ending after June 30, 1950 (whether or not the credit for such taxable year is computed under section 435) shall be computed without regard to the net operating loss for any taxable year ending before July 1, 1950. The net operating loss carry-over specified in this paragraph shall not be allowed as a net operating loss carry-over to any taxable year for which the excess profits credit is not computed under section 435 (relating to the excess profits credit based on income) and is not computed under section 436 (a) by use of the historical invested capital determined under section 458.

(3) The application of section 433 (a) (1) (J) (iii)–(v) may be illustrated as follows:

The X Corporation which makes its returns on the basis of the calendar year had net income (as defined in section 437 (f) (2) (B)) and net operating losses (as defined in section 437 (f) (2) (A)), for the calendar years 1944 to 1949, inclusive, as follows:

| | Net income | Net operating loss |
|---|---|---|
| Years preceding base period: | | |
| 1944 | $100,000 | |
| 1945 | 50,000 | |
| Base period years: | | |
| 1946 | | ($350,000) |
| 1947 | 90,000 | |
| 1948 | | (15,000) |
| 1949 | 40,000 | |

For the purpose of section 433 (a) (1) (J), the net operating loss for 1946 is limited to the amount of the net operating loss carry-over from 1946 to 1947, or $200,000 ($350,000 minus the sum of $100,000 and $50,000). The sum of the $200,000 net operating loss so computed for 1946 and the $15,000 net operating loss for 1948, or $215,000, exceeds the sum of the net income for the base period years ($90,000 for 1947 and $40,000 for 1949, or a total of $130,000) by $85,000. If the excess profits credit for 1950 is determined under section 435 or under section 436 (a) by the use of section 458, the $85,000 so computed may, at the election of the taxpayer made on its return for 1950, be treated as a net operating loss carry-over from 1949, and the $85,000 carry-over will, subject to the provisions of section 122 (b) (2), be a carry-over to the years 1950 and 1951. The net operating loss deduction for 1950 is determined without regard to any other carry-over from a taxable year ending before June 30, 1950, for example the loss for 1948 if such loss exceeded the net income for 1949, and the net operating loss deduction for any subsequent taxable year for which the excess profits credit is computed under neither section 435 nor section 458 is determined without regard to the $85,000 carry-over from the base period. If the taxpayer had a net operating loss for 1950, the amount of the carry-over from 1950 to 1951 and subsequent taxable years would be the net operating loss for 1950 reduced by the net income for 1949, the computation of such net income being unaffected by the determination of a net operating loss carry-over from 1949 under section 433 (a) (1) (J) (iii).

(k) Section 433 (a) (1) (K) provides that if, under a lease for a term of more than 20 years entered into prior to December 1, 1950, the lessee is obligated to pay any portion of the tax imposed by chapter 1 upon the lessor with respect to the rentals derived by such lessor from such lessee, or is obligated to reimburse the lessor for any portion of the tax imposed by chapter 1 upon the lessor with respect to the rentals derived by such lessor from such lessee, such payment or reimbursement of the tax imposed by chapter 1 shall be excluded by the lessor, and a deduction therefor shall not be allowed to the lessee, in computing excess profits net income. For this purpose, an agreement for lease of railroad properties entered into prior to December 1, 1950, shall be considered to be a lease including such term as the total number of years such agreement may, unless sooner terminated, be renewed or continued under the terms of the agreement, and any such renewal or continuance under such agreement shall be considered part of the lease entered into prior to December 1, 1950.

(l) In the case of a bank (as defined in section 104) using the reserve method of accounting for bad debts, section 433 (a) (1) (L) requires an adjustment to normal-tax net income equal to the difference between (1) the amount of the deduction for additions to the reserve for bad debts allowed under section 23 (k) (including, in the case of the taxable year in which the reserve is established, the deduction for the initial credit to the reserve) and (2) the amount that would have been allowable as a deduction under section 23 (k) for bad debts for the taxable year if the bank did not use the reserve method of accounting for bad debts. The adjustment is effected by increasing normal-tax net income by the amount of the deduction allowed under section 23 (k) for the additions to the bad debt reserve for the taxable year and by decreasing normal-tax net income by the amount of the deduction which would be allowable under section 23 (k) for the debts which actually became worthless in the taxable year, in whole or in part.

(m) Section 433 (a) (1) (M) provides for the exclusion of income derived from sources within any foreign country to the extent that such income would, but for monetary, exchange, or other restrictions imposed by such foreign country, have been includible in the gross income of the taxpayer for any taxable year which preceded its first taxable year ended after June 30, 1950. If such foreign income is includible in the gross income of the taxpayer for a taxable year succeeding the first taxable year ended after June 30, 1950, and, but for such restrictions, would have been includible in the gross income of the taxpayer for its first taxable year ended after June 30, 1950, and if such first taxable year began prior to July 1, 1950, such income shall be excluded in an amount which is the same proportion of such income as the number of days prior to July 1, 1950, in such first taxable year is of the total number of days in such first taxable year. Deductions properly chargeable and allocable to the income excluded under section 433 (a) (1) (M) shall not be allowed.

(n) An adjustment for interest on borrowed capital is provided in section 433 (a) (1) (N) in the case of a taxpayer computing its excess profits credit under section 436 (the invested capital method). This adjustment may be illustrated by the case of a taxpayer which has interest of $10,000 for the taxable year on indebtedness which constitutes borrowed capital for such taxable year, such interest of $10,000 being deducted by the taxpayer in computing normal-tax net income. Section 433 (a) (1) (N) requires that 75 percent of this amount, or $7,500, be added to normal-tax net income in computing excess profits net income.

(o) An adjustment for interest on borrowed capital is provided in section 433 (a) (1) (O) in the case of a taxpayer computing its excess profits credit for the taxable year under section 435 (the income method). For example, if the taxpayer referred to in (n) of this section computes its excess profits credit for the taxable year under section 435, if its average borrowed capital for the taxable year was $300,000, and if this amount exceeds by $100,000 its borrowed capital at the beginning of its first taxable year ending after June 30, 1950, then 75 percent of such excess, or $75,000, is the increase in borrowed capital under section 435 (g) (3) (C). If the average of its loans to members of a controlled group for the taxable year is $25,000, and if this amount exceeds by $20,000 the amount of such loans on the first day of its first taxable year ending after June 30, 1950, then 75 percent of such excess, or $15,000, is the amount determined by reference to section 435 (g) (4) (E). The excess of the $75,000 determined under section 435 (g) (3) (C) over the $15,000 determined under section 435 (g) (4) (E), or $60,000, is 20 percent of its average borrowed capital of $300,000 for the taxable year. Accordingly, section 433 (a) (1) (O) requires that excess profits net income be computed by increasing normal-tax net income by 20 percent of the $10,000 deduction for interest on borrowed capital, or $2,000.

(p) Special adjustments to normal-tax net income are required in the case of a taxpayer which has received a grant or loan described in section 433 (a) (1) (P) from the United States (or from any agency or instrumentality of the United States) for the encouragement of exploration, development, or mining of critical and strategic minerals or metals.

(q) For adjustments under section 433 (a) (1) (Q), in the case of a taxpayer making the election provided in section 455 with respect to income derived from installment sales, installment sales obli-

gations, or long-term contracts, see section 455.

§ 40.433 (a)–3 *Tax for period of less than 12 months*—(a) *Methods of computing tax for short taxable year; allowance.* Section 433 (a) (2) provides rules, under a general rule and under an exception to such rule, which are applicable to short taxable years for the purpose of determining 12 months' experience and computing the excess profits tax for such year. A short taxable year is any taxable period of less than 12 months. If the period from the date of incorporation of a corporation to the end of its first accounting period, or the period from the beginning of its last accounting period to the date it ceases operations and is dissolved, retaining no assets, is a period of less than 12 months, such period is a short taxable year. The tax imposed by section 430 (a) for the short taxable year shall be computed under paragraph (b) of this section, except as otherwise provided in paragraph (c) of this section. The provisions of section 47 (c) are not applicable to the excess profits tax.

(b) *General rule.* Section 433 (a) (2) (A) provides that the excess profits net income for a short taxable year shall be placed on an annual basis by multiplying the amount thereof by the number of days in the 12 months ending with the close of the short taxable year and dividing by the number of days in the short taxable year. A tentative tax shall then be computed under section 430 (a) as though the excess profits net income were the amount so ascertained under the preceding sentence. The tentative tax is the tax so computed under paragraph (1) or (2) of section 430 (a), whichever is the lesser amount. The actual tax for the short taxable year shall be an amount which bears the same ratio to such tentative tax as the number of days in the short taxable year bears to the total number of days in the 12 months ending with the close of the short taxable year.

(c) *Exception; tax for short period determined by actual 12-month adjusted excess profits net income.* (1) If the taxpayer applies to the Commissioner in the manner provided in paragraph (d) of this section to have its tax computed under the provisions of section 433 (a) (2) (B), and if the taxpayer establishes the amount of its adjusted excess profits net income, computed for the 12-month period hereinafter described and under the rules hereinafter prescribed, then section 433 (a) (2) (B) provides that the tax for the short taxable year shall be reduced to an amount which is such part of the tax computed on the basis of the adjusted excess profits net income which the taxpayer has established for such 12-month period as the excess profits net income for the short taxable year is of the excess profits net income for such 12-month period. If such amount, however, is greater than the tax computed under paragraph (b) of this section, the tax for the short taxable year is the tax computed under paragraph (b) of this section. The 12-month period referred to above is the 12-month period beginning with the first day of the short taxable year, except that if the taxpayer has disposed of substantially all its assets prior to the end of such 12-month period, then it is the 12-month period ending with the last day of the short taxable year. If a corporation ceases business and distributes so much of the assets used in its business that it cannot resume its customary operations with the remaining assets, it has disposed of substantially all of its assets.

(2) In computing the tax under section 433 (a) (2) (B), the excess profits net income for the short taxable year is not placed on an annual basis as provided in section 433 (a) (2) (A). The adjusted excess profits net income for the 12-month period is computed under the same provisions of law as are applicable to the short taxable year, with the use of the credits applicable in determining the adjusted excess profits net income for such short taxable year (as if this section were not applicable), and is computed as if the 12-month period were an actual accounting period of the taxpayer. All items which fall in such 12-month period must be included even if they are extraordinary in amount or of an unusual nature. The adjustments provided in section 433 (a) (1) under the law applicable to such short taxable year shall be made upon the basis of the normal-tax net income for such 12-month period. The apportionment of items to such 12-month period shall be made in accordance with the method and principles applicable under § 29.47–2 (b) of Regulations 111. The excess profits net income for the 12-month period used shall in no case be considered less than the actual excess profits net income for the short taxable year.

(d) *Application to compute tax under section 433 (a) (2) (B).* A taxpayer desiring the benefit of section 433 (a) (2) (B) must file an application therefor. If at the time the return for the short taxable year is filed the taxpayer is able to determine that the 12-month period ending with the close of the short taxable year will be used in the computations under section 433 (a) (2) (B), then the tax on the return for the short taxable year may be determined under the provisions of section 433 (a) (2) (B). In such a case, an excess profits tax schedule covering the 12-month period shall be attached to the return as a part thereof, and the return will then be considered the application for the benefits of section 433 (a) (2) (B) required by that section. In all other cases, the taxpayer shall file its return and compute its tax as provided in (b) of this section, and the application for the benefit of section 433 (a) (2) (B) shall be made in the form of a claim for credit or refund if the tax computed under section 433 (a) (2) (A) has been paid, or, if the tax computed under section 433 (a) (2) (A) has not been paid, the application shall consist of a notice to the Commissioner setting forth the facts involved together with an excess profits tax schedule covering the 12-month period used. The claim or other application for the benefit of section 433 (a) (2) (B) shall set forth the computation of the adjusted excess profits net income and the tax thereon for the 12-month period and, if credit or refund is sought for taxes paid before the application for the benefit of section 433 (a) (2) (B) is filed, the claim must be filed not later than June 15, 1951, or the time prescribed for filing the return for the first taxable year (or for the period which would be its taxable year if it continued in existence) ending with or after the twelfth month after the beginning of the short taxable year, whichever date is later. For example, the taxpayer changes its accounting period from the calendar year to the fiscal year ending September 30, and files a return for the period from January 1, 1950, to September 30, 1950. At the time it files its return, it pays the tax computed thereon under the provisions of section 433 (a) (2) (A). Its claim for credit or refund of the overpayment which would result from the application of section 433 (a) (2) (B) must be filed not later than the time prescribed for filing its return for the first taxable year which ends on or after the last day of December 1950, the twelfth month after the beginning of the short taxable year. In this case, the taxpayer must file its claim for credit or refund not later than December 15, 1951, the time prescribed for filing the return for its fiscal year ending September 30, 1951. However, if it obtains an extension of time for filing the return for such fiscal year, it may file its claim during the period of such extension. If the Commissioner determines that the taxpayer has established the amount of the adjusted excess profits net income for the 12-month period, any excess of the tax paid for the short taxable year over the tax computed under section 433 (a) (2) (B) will be credited or refunded to the taxpayer in the same manner as in the case of any other overpayment. An application for the benefit of section 433 (a) (2) (B), other than a claim for credit or refund, made in any case in which the tax liability computed under section 433 (a) (2) (A) has not been paid, may be filed at any time before the tax liability for the taxable year is finally determined. Such application does not constitute a claim for credit, refund, or abatement. If credit or refund is sought for taxes paid after such application is filed, a claim therefor on Form 843 should be filed after such payment and within the period prescribed in section 322.

SEC. 433. EXCESS PROFITS NET INCOME.

* * * * *

(b) *Taxable years in base period.* For the purposes of computing the average base period net income, the excess profits net income for any taxable year shall be the normal-tax net income, as defined in section 13 (a) (2) as in effect for such taxable year, increased or decreased by the following adjustments (for additional adjustments in case of certain reorganizations, see part II of this subchapter):

(1) *Net operating loss deduction.* The net operating loss deduction provided by section 23 (s) shall not be allowed;

(2) *Gains and losses from sales or exchanges of capital assets, etc.* There shall be excluded gains and losses from sales or exchanges of capital assets and gains and losses to which section 117 (j) is applicable;

(3) *Income from retirement or discharge of bonds, etc.* There shall be excluded, in

the case of any taxpayer, income derived from the retirement or discharge by the taxpayer of any bond, debenture, note, or certificate or other evidence of indebtedness, if the obligation of the taxpayer has been outstanding for more than 6 months, including, in case the issuance was at a premium, the amount includible in income for such year solely because of such retirement or discharge;

(4) *Deductions on account of retirement or discharge of bonds, etc.* If during the taxable year the taxpayer retires or discharges any bond, debenture, note, or certificate or other evidence of indebtedness, if the obligation of the taxpayer has been outstanding for more than 6 months, the following deductions for such taxable year shall not be allowed:

(A) The deduction allowable under section 23 (a) for expenses paid or incurred in connection with such retirement or discharge;

(B) The deduction for losses allowable by reason of such retirement or discharge; and

(C) In case the issuance was at a discount, the amount deductible for such year solely because of such retirement or discharge;

(5) *Repayment of processing tax to vendees.* The deduction under section 23 (a), for any taxable year, for expenses shall be decreased by an amount which bears the same ratio to the amount deductible on account of any repayment or credit by the corporation to its vendee of any amount attributable to any tax under the Agricultural Adjustment Act of 1933, as amended, as the excess of the aggregate of the amounts so deductible in the base period over the aggregate of the amounts attributable to taxes under such Act collected from its vendees which were includible in the corporation's gross income in the base period and which were not paid, bears to the aggregate of the amounts so deductible in the base period;

(6) *Dividends received.* The credit for dividends received shall apply, without limitation (except the limitation relating to dividends in kind), to all dividends on stock of all corporations, except that no credit for dividends received shall be allowed with respect to dividends (actual or constructive) on stock of foreign personal holding companies or dividends on stock which is not a capital asset;

(7) *Installment sales.* In the case of a taxpayer which has made the election provided in section 455 (a), income from installment sales and from installment sales obligations shall be computed (in lieu of in the manner provided in section 44) under the accrual method without treating any portion of such income as unrealized at the close of any period and as if the taxpayer had reported such income on such accrual method for all taxable periods.

(8) *Long-term contracts.* In the case of a taxpayer which has made the election provided in section 455 (b), income from long-term contracts shall be computed under the percentage of completion method and as if the taxpayer had reported such income on the percentage of completion method for all taxable periods.

(9) *Judgments, intangible drilling and development costs, casualty losses, and other abnormal deductions.* If, for any taxable year or years within, or beginning or ending within, the base period, any class of deductions for the taxable year exceeded 115 per centum of the average amount of deductions of such class for the four previous taxable years (not including deductions arising from the same extraordinary event which gave rise to the deduction for the taxable year), the deductions of such class shall, subject to the rules provided in paragraph (10), be disallowed in an amount equal to such excess. For the purposes of this paragraph, each of the following groups of deductions shall constitute a class of deductions:

(A) Deductions attributable to claims, awards, judgments, and decrees against the taxpayer, and interest on the foregoing;

(B) Deductions attributable to intangible drilling and development costs paid or incurred in or for the drilling of wells or the preparation of wells for the production of oil or gas, and for development costs in the case of mines; and

(C) Deductions under section 23 (f) for losses arising from fires, storms, shipwreck, or other casualty, or from theft, or arising from the demolition, abandonment, or loss of useful value of property, not compensated for by insurance or otherwise. The class of deductions under this subparagraph for any taxable year shall not include deductions which are excludible under paragraph (2) or which would be so excludible if such paragraph were applicable with respect to such taxable year.

The classification of deductions of any class not described in subparagraphs (A) to (C), inclusive, shall be subject to regulations prescribed by the Secretary.

(10) *Rules for application of paragraph (9).* For the purpose of paragraph (9)—

(A) If the taxpayer was not in existence for four previous taxable years, then the average amount specified in such paragraph shall be determined for the previous taxable years it was in existence and the succeeding taxable years which begin before the beginning of the taxpayer's second taxable year under this subchapter. If the number of such succeeding years is greater than the number necessary to obtain an aggregate of four taxable years, there shall be omitted so many of such succeeding years, beginning with the last, as are necessary to reduce the aggregate to four.

(B) Deductions of any class for any taxable year shall not be disallowed under such paragraph unless the amount of deductions of such class to be disallowed for such year exceeds 5 per centum of the average excess profits net income for the taxable years within, or beginning or ending within, the base period, computed without the disallowance of any class of deductions under such paragraph. Such average excess profits net income shall, for the purposes of this subparagraph, be computed by aggregating the excess profits net incomes of all such taxable years, dividing such aggregate by the total number of months in such years, and multiplying the quotient by 12. For the purposes of this subparagraph, the excess profits net income for any taxable year shall in no case be less than zero.

(C) Deductions of any class shall not be disallowed under such paragraph unless the taxpayer establishes that the increase in such deductions—

(i) Is not a cause or a consequence of an increase in the gross income of the taxpayer in its base period or a decrease in the amount of some other deduction in its base period, which increase or decrease is substantial in relation to the amount of the increase in the deductions of such class, and

(ii) Is not a consequence of a change at any time in the type, manner of operation, size, or condition of the business engaged in by the taxpayer.

(D) The amount of deductions of any class to be disallowed under such paragraph with respect to any taxable year shall not exceed the amount by which the deductions of such class for such taxable year exceed the deductions of such class for the taxable year for which the tax under this subchapter is being computed.

(11) *Taxes paid by lessee.* If under a lease for a term of more than 20 years entered into prior to December 1, 1950, the lessee is obligated to pay any portion of the tax imposed by this chapter upon the lessor with respect to the rentals derived by such lessor from such lessee, or is obligated to reimburse the lessor for any portion of the tax imposed by this chapter upon the lessor with respect to the rentals derived by such lessor from such lessee, such payment or reimbursement of the tax imposed by this chapter shall be excluded by the lessor and a deduction therefor shall not be allowed to the lessee. For the purposes of this paragraph an agreement for lease of railroad properties entered into prior to December 1, 1950, shall be considered to be a lease including such term as the total number of years such agreement may, unless sooner terminated, be renewed or continued under the terms of the agreement, and any such renewal or continuance under such agreement shall be considered part of the lease entered into prior to December 1, 1950.

(12) *Bad debts in case of banks.* In the case of a bank (as defined in section 104) using the reserve method of accounting for bad debts, there shall be allowed, in lieu of the amount allowable under the reserve method for bad debts, a deduction for debts which became worthless within the taxable year, in whole or in part, within the meaning of section 23 (k).

(13) *Bank assessments by Federal Deposit Insurance Corporation.* In the case of a bank (as defined in section 104), the deduction for the assessment by the Federal Deposit Insurance Corporation shall be reduced to an amount which is such part thereof as the net assessment (after credits applicable thereto) for the taxable year for which the excess profits credit is being computed is of the gross assessment for such taxable year.

(14) *Life insurance companies.* In the case of a life insurance company, there shall be deducted from the normal-tax net income the excess of (A) the product of (i) the figure determined and proclaimed under section 202 (b) and (ii) the excess profits net income computed without regard to this paragraph, over (B) the adjustment for certain reserves provided in section 202 (c).

(15) *Credit for income subject to prior excess profits tax.* The credit provided in section 26 (e) shall not be allowed.

(c) *Deficit in excess profits net income.* For the purposes of this subchapter, the deficit in excess profits net income for any taxable year shall be the excess, if any, of—

(1) The sum of the deductions from gross income, the credit for dividends received, the credit provided in section 26 (a) (relating to interest on certain obligations of the United States and its instrumentalities) and the amount of the decrease resulting from the adjustments provided in subsection (b), over

(2) The sum of the gross income and the amount of the increase resulting from the adjustments provided in subsection (b).

§ 40.433 (b)-1 *Excess profits net income used in computing average base period net income.* (a) For the purpose of determining the excess profits credit for the taxable year under section 435, the excess profits net income for each taxable year within the base period, for each taxable year beginning before the base period and ending within the base period, and for each taxable year beginning within the base period and ending after the base period, must be computed under section 433 (b). Furthermore, the excess profits net income for certain taxable years beginning after the base period must also be computed under section 433 (b) for the purpose of applying section 435 (e). In general, wherever excess profits net income is a factor in computing average base period net income, such excess profits net income must be computed under section 433 (b). Excess profits net income is computed under section 433 (a) for the purpose of determining the amount

referred to in section 431, relating to adjusted excess profits net income, from which amount the excess profits credit and unused excess profits credit adjustment are substracted in order to determine the adjusted excess profits net income. Thus, in the case of a taxable year beginning in the base period and ending after June 30, 1950, the excess profits net income for such taxable year referred to in section 431 is computed under section 433 (a) in order to determine the adjusted excess profits net income for such taxable year, and the excess profits net income for such taxable year is also computed under section 433 (b) for the purpose of determining the average base period net income used in determining the excess profits credit of the taxpayer for that year and for subsequent taxable years.

(b) The base period is the period beginning January 1, 1946, and ending December 31, 1949, except that in the case of a taxpayer whose first taxable year ending after June 30, 1950, was preceded by a taxable year which began in 1949 and ended after December 31, 1949, and before April 1, 1950, the base period is the 48 consecutive months which ended with the close of such preceding taxable year. See section 435 (b).

(c) The starting point in the determination of the excess profits net income for any taxable year under section 433 (b) is the normal-tax net income for such taxable year computed under the provisions of section 13 (a) (2) applicable to such taxable year. Such normal-tax net income for the taxable year is then increased or decreased by the adjustments specified in section 433 (b). For additional adjustments in case of certain reorganizations, see sections 461–465. In the case of a taxpayer which has made the election provided in section 455 (a), relating to income from installment sales and from installment sales obligations, or has made the election provided in section 455 (b), relating to income from long-term contracts, the normal-tax net income referred to above is first recomputed as if the taxpayer had for all taxable periods reported such income under the method of accounting elected under section 455.

§ 40.433 (b)–2 *Computation of excess profits net income.* (a) Several of the adjustments required by section 433 (b) in determining excess profits net income correspond to adjustments required by section 433 (a), and such adjustments shall be made in a manner corresponding to that provided under section 433 (a). These are (1) the adjustment for income from retirement or discharge of bonds, etc., (2) the adjustment for deductions on account of retirement or discharge of bonds, etc., (3) the adjustment for dividends received, (4) the adjustment for income from installment sales and from installment sales obligations in the case of a taxpayer which has made the election provided in section 455 (a), (5) the adjustment for income from long-term contracts in the case of a taxpayer which has made the election provided in section 455 (b), (6) the adjustment for taxes paid by a lessee under certain types of leases, (7) the adjustment for bad debts in the case of a bank using the reserve method of accounting for bad debts, and (8) the adjustment to income in the case of life insurance companies.

(b) Section 433 (b) (1) provides that the net operating loss deduction provided by section 23 (s) shall not be allowed in the computation of excess profits net income. This necessitates the addition to normal-tax net income of the amount of the net operating loss deduction, if any, which was allowed in computing such normal-tax net income.

(c) Section 433 (b) (2) requires that normal-tax net income be adjusted by the exclusion therefrom of gains and losses from sales or exchanges of capital assets (whether long-term or short-term) and gains and losses to which section 117 (j) is applicable. This adjustment requires the decrease of normal-tax net income by the amount of the net capital gain of the corporation included in computing normal-tax net income. No adjustment is required in the case of a net capital loss of the corporation which is not deducted in computing normal-tax net income. If the gains described in section 117 (j) exceed the losses therein described, such gains and losses are capital gains and losses included in determining net capital gain or loss. However, if such losses exceed (or equal) such gains, such gains and losses are not capital gains and losses, and normal-tax net income must be increased by the amount of such excess, if any, since the inclusion of such gains and losses in computing normal-tax net income reduced it by the amount of such excess.

(d) Under section 433 (b) (15) the credit provided in section 26 (e) is not allowed in computing excess profits net income for a taxable year in the base period. Thus, if a credit for income subject to excess profits tax has been deducted in computing the normal-tax net income for a taxable year beginning in 1945, the normal-tax net income for such taxable year must be increased by the amount of such credit in computing excess profits net income.

(e) For the purpose of the adjustments under section 433 (b) (3) and under section 433 (b) (4), relating to income and deductions from the retirement or discharge of bonds, etc., the obligation of the taxpayer must have been outstanding for more than six months. In making the adjustments provided in section 433 (b) (4), the deduction allowable for any premium paid on bonds when called for redemption shall be disallowed, but the deduction allowable for any discount amortized up to the date of retirement or discharge shall not be disallowed. Expenses incurred in issuing bonds which are amortized shall be treated in the same manner as discounts.

(f) In the case of a bank (as defined in section 104), section 433 (b) (13) provides an adjustment with respect to the deduction allowed for assessments by the Federal Deposit Insurance Corporation. Excess profits net income is computed in the case of a bank by increasing normal-tax net income by the excess of such deduction over an amount which is such part thereof as the net assessment (after credits applicable thereto) by the Federal Deposit Insurance Corporation for the taxable year for which excess profits tax is being computed is of the gross assessment for such taxable year. For example, if the gross assessment for the taxable year for which the tax is being computed is subject to a credit in an amount equal to 60 percent thereof, then excess profits net income for the base period taxable year is computed by increasing normal-tax net income for such base period taxable year by an amount equal to 60 percent of the deduction allowed for such base period taxable year for assessments by the Federal Deposit Insurance Corporation.

§ 40.433 (b)–3 *Abnormal deductions in base period*—(a) *Nature of adjustments.* Section 433 (b) (9) and (10) provides adjustments in computing excess profits net income for certain classes of deductions. The first step in determining such adjustments is the computation of the amount by which such a class of deductions for the taxable year exceeds 115 percent of the average amount of such class for the four immediately preceding taxable years. If the taxpayer was not in existence for four immediately preceding taxable years, then the average amount of deductions of any class shall be determined for the preceding taxable years during which it was in existence and the succeeding taxable years which begin before the beginning of the taxpayer's second excess profits tax taxable year. If the number of such succeeding taxable years is greater than the number necessary to obtain an aggregate of four taxable years, there shall be omitted as many of the succeeding years, beginning with the last, as are necessary to reduce the aggregate to four. For example, in the case of a corporation coming into existence on January 1, 1947, and making its return on the basis of the calendar year, the amount of deductions of any class which may be disallowed for the taxable year 1949 may be determined from the average of the deductions for 1947, 1948, and 1950. The taxable year 1951 is the taxpayer's second excess profits tax taxable year and therefore may not be used.

(b) *Extraordinary event.* If an extraordinary event gives rise to deductions of the same class for more than one taxable year, then in determining whether the deductions of such class exceed 115 percent of the average deductions of that class, such average shall be computed without reference to any deductions attributable to the extraordinary event. For example, if an extraordinary fire in 1948 caused by the negligence of a corporation results, both in 1948 and 1949, in judgments against the corporation in favor of persons injured by the fire, then in determining whether the amount of the class of deductions by the corporation for judgments, awards, etc., for the taxable year 1949 exceeds 115 percent of the amount of the average deductions of that class for the four preceding taxable years, the deductions for such judgments in 1948 are not taken into account in computing the average deductions for such four preceding years.

(c) *Additional requirements.* Even though a taxpayer has a class of deductions for a taxable year which meets the requirement that it exceed 115 percent of the average of such class of deductions for the taxable years used in determining average deductions, the taxpayer will not be entitled to compute excess profits net income by adding such excess to normal-tax net income unless the following additional requirements are also met:

(1) The amount of such excess must exceed 5 percent of the average excess profits net income for the taxable years which are within, which begin within, and which end within the base period (computed without the disallowance of any such class of deductions). Such average excess profits net income shall, for this purpose, be computed by aggregating the excess profits net incomes of all such taxable years, dividing such aggregate by the total number of months in such years, and multiplying the quotient by 12. For this purpose, the excess profits net income for any taxable year shall in no case be considered less than zero.

(2) The taxpayer must establish that the increase in the deductions of the class, which increase results in such excess, (i) is not the cause or consequence of (A) an increase in the gross income of the taxpayer in the base period which is substantial in relation to the amount of the increase in the deductions of that class, or (B) a decrease in the amount of some other deduction of the taxpayer in the base period which is substantial in relation to the increase in the deductions of the class, and (ii) is not a consequence of a change at any time in the type, manner of operation, size, or condition of the business engaged in by the taxpayer.

Furthermore, the amount of the excess disallowed may not exceed the amount by which the deductions of such class for such taxable year exceed the deductions of such class for the taxable year for which the excess profits tax is being computed.

(d) *Classification of deductions.* (1) In section 433 (b) (9) (A), (B), and (C), there are described three groups of deductions, each of which is specifically declared to be a class of deductions. These three classes are:

(i) Deductions attributable to claims, awards, judgments, and decrees against the taxpayer, and interest on the foregoing.

(ii) Deductions attributable to intangible drilling and development costs paid or incurred in or for the drilling of wells or the preparation of wells for the production of oil or gas, and for development costs in the case of mines. Deductions attributable to the operation of wells or mines are not included in this class.

(iii) Deductions under section 23 (f) for losses arising from fires, storms, shipwreck, or other casualty, or from theft, or arising from the demolition, abandonment, or loss of useful value of property, not compensated for by insurance or otherwise. This class of deductions for any taxable year shall not include deductions which are excludible under section 433 (b) (2) or which would be so excludible if section 433 (b) (2) were applicable with respect to such taxable year. Accordingly, this class of deductions for any taxable year does not include losses described in section 117 (j) and does not include capital losses.

(2) Deductions which do not fall within any of the classes specified in section 433 (b) (9) (A)–(C) may be grouped by the taxpayer, subject to approval by the Commissioner on the examination of the taxpayer's return, in such other classes as are reasonable in a business of the type which the taxpayer conducts and are applicable in the light of the taxpayer's business experience and accounting practice. Such a classification will be applicable to all other taxable years considered at any time in adjusting deductions under this section.

(3) For the purpose of determining whether a particular class of deductions exceeds 115 percent of average deductions of the same class, reference must be made to the deductions of the entire class rather than to any particular deductible items included therein.

(e) *Statement required.* If in computing its excess profits net income under section 433 (b), the taxpayer claims the disallowance under section 433 (b) (9) or (10) of any amount previously allowed as a deduction, there shall be submitted a full statement showing the computation of the amount to be disallowed, the prices and gross sales of the taxpayer's product, and the condition of the taxpayer's business which demonstrate that the disallowed amount is not a cause or a consequence of an increase in the gross income of the taxpayer in its base period or a decrease in the amount of some other deduction in its base period, and is not a consequence of a change at any time in the type, manner of operation, size, or condition of the business engaged in by the taxpayer. This statement shall be in duplicate and shall include the following: (1) The computation of the amount disallowed, showing the amount of the class of deductions in the base period taxable year for which any part of such amount is disallowed, the average amount of such class for the four preceding taxable years or for such taxable years as the taxpayer is required to use in determining this average amount, and the excess amount of deductions disallowed; (2) a computation showing (i) the excess profits net income for each taxable year which is within, which begins within, and which ends within, the base period, computed without the disallowance of any class thereof, (ii) the average of such excess profits net income computed in accordance with section 433 (b) (10) (B), and (iii) the amount of 5 percent of such average excess profits net income so computed; (3) a description and the amount of each item included in such class of deductions for the taxable year for which such deductions are disallowed and for the taxable years in the test period, with the amount of each and a description thereof; (4) the amount of such class and the amount and description of each item in that class for the taxable year for which the excess profits tax is being computed; and (5) all other facts upon which the taxpayer relies.

SEC. 434. EXCESS PROFITS CREDIT—ALLOWANCE.

(a) *Domestic corporations.* In the case of a domestic corporation, the excess profits credit for any taxable year shall be an amount computed under section 435 or section 436, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed.

(b) *Foreign corporations.* In the case of a foreign corporation engaged in trade or business within the United States, the first taxable year of which under this subchapter begins on or before July 1, 1950, which was in existence on January 1, 1946, and which at any time during each of the taxable years which began or ended during the base period was engaged in trade or business within the United States, the excess profits credit for any taxable year shall be an amount computed under section 435 or section 436, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of all other foreign corporations the excess profits credit for any taxable year shall be an amount computed under section 436 (b).

(c) *Special rule in connection with regulated public utilities.* Notwithstanding subsection (a), in the case of a regulated public utility (as defined in section 448) the excess profits credit for any taxable year shall be an amount computed under section 435, section 436, or section 448, whichever results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of a regulated public utility which has made and filed a consent described in section 141 (e) (8) or (j) applicable to the taxable year, the excess profits shall, for purposes of filing a consolidated return, be determined in accordance with such consent.

(d) *Special rule for railroad lessor-lessee corporations.* Notwithstanding the provisions of subsection (a) or (c), in the case of a railroad corporation subject to Part I of the Interstate Commerce Act, substantially all of the railroad properties of which have been leased to another such railroad corporation or corporations by an agreement or agreements entered into prior to December 1, 1950, where each lease is for a term of more than 20 years and where under one or more of the leases or agreements relating to the leased properties the lessee is, or the lessees are, required to pay the taxes of the lessor under this chapter, the aggregate of the excess profits credit and the unused excess profits credit adjustment of each of such corporations, computed without regard to this subsection, may be equitably apportioned among the lessor and each of the lessee corporations so required to pay the taxes of the lessor under this subchapter by agreement among such corporations approved by the Secretary. For the purposes of this subsection an agreement for lease of railroad properties entered into prior to December 1, 1950, shall be considered to be a lease including such term as the total number of years such agreement may, unless sooner terminated, be renewed or continued under the terms of the agreement, and any such renewal or continuance under such agreement shall be considered part of the lease entered into prior to December 1, 1950.

§ 40.434–1 *Excess profits credit; allowance*—(a) *In general.* (1) For domestic corporations, two general methods are provided for computing the excess profits credit: (i) The income method (including the provisions of section 442 through 446) under section 435; and (ii) the invested capital method (including the historical invested capital method pro-

vided in section 458) under section 436. An alternative credit is provided in section 448 in the case of certain regulated public utilities. See paragraph (b) of this section. A domestic corporation shall use whichever of these credits produces the lowest excess profits tax.

(2) For computation of the excess profits credit based on income in the case of a corporation which has been a party to a transaction described in section 461 (a), see sections 461 through 465. For computation of the excess profits credit based on invested capital in the case of a corporation which has been a party to certain reorganizations, exchanges, and intercorporate liquidations, see sections 470 through 472. A corporation entitled to the benefits of section 251 may compute its credit by using either the income method under section 435 or the invested capital method under section 436 (b).

(b) *Regulated public utilities.* An additional alternative method of computing its credit is provided for a regulated public utility, as defined in section 448. In such a case the excess profits credit for any taxable year shall be an amount computed under section 435, 436, or 448, whichever results in the lowest tax for the taxable year for which the tax is being computed. In the case of a regulated public utility which has made and filed a consent described in section 141 (e) (8) or (j) applicable to the taxable year, the excess profits credit shall, for purposes of filing a consolidated return, be determined in accordance with such consent.

(c) *Foreign corporations.* A foreign corporation is required to compute its credit under the invested capital method as provided in section 436 (b) except that a foreign corporation (1) which is engaged in trade or business within the United States at any time during the taxable year, (2) the first taxable year of which for the purposes of the excess profits tax began on or before July 1, 1950, (3) which was in existence on January 1, 1946, and (4) which, at any time during each of the taxable years which began or ended during the base period defined in section 435 (b) was engaged in trade or business within the United States, may also compute its credit under the income method and shall use whichever credit produces the lower excess profits tax. As to what constitutes being engaged in a trade or business within the United States, see § 29.231–1 of Regulations 111.

(d) *Railroad lessor-lessee corporations.* (1) If substantially all the railroad properties of a railroad corporation subject to Part I of the Interstate Commerce Act have been leased for a term of more than 20 years to another such railroad corporation or corporations pursuant to an agreement or agreements entered into prior to December 1, 1950, which agreement or agreements require the lessee or lessees to pay the taxes of the lessor, the aggregate of the excess profits credit and the unused excess profits credit adjustment of each such corporation may be equitably apportioned by agreement, if approved by the Commissioner, among the lessor and each of the lessee corporations so required to pay the taxes of the lessor. The term of a lease of railroad properties entered into prior to December 1, 1950, shall, for the purpose of the preceding sentence, be deemed to include the years for which such lease may be renewed or continued.

(2) The original agreement for such equitable apportionment shall be filed with the collector by the lessor railroad corporation, and a duplicate original shall be filed with the collector by the lessee (or by each lessee, if more than one) railroad corporation. Subject to subsequent approval by the Commissioner, a taxpayer which has made such an agreement may compute its tax on its return pursuant to such agreement, provided that the original agreement, or a duplicate original, as the case may be, is attached to the return together with a statement clearly showing the proper computation of the tax without regard to the agreement. If the return is filed without regard to the agreement, the original agreement (or a duplicate original in the case of a lessee) shall be attached to a claim for refund if the application of section 434 (d) results in an overpayment, or to an amended return if the application of section 434 (d) does not result in an overpayment.

SEC. 435. EXCESS PROFITS CREDIT—BASED ON INCOME.

(a) *Amount of excess profits credit.* The excess profits credit for any taxable year, computed under this section, shall be—

(1) *Domestic corporations.* In the case of a domestic corporation the sum of—

(A) 85 per centum of the average base period net income,

(B) If the average base period net income of the taxpayer is the amount determined under subsection (d) of this section or under section 442, 12 per centum of the amount of the base period capital addition, computed under subsection (f), and

(C) 12 per centum of the net capital addition (as defined in subsection (g) (1)) for the taxable year,

minus 12 per centum of the net capital reduction (as defined in subsection (g) (2)) for the taxable year.

(2) *Foreign corporations.* In the case of a foreign corporation, 85 per centum of the average base period net income.

(3) *Cross reference.* For the computation of the excess profits credit based on income in the case of certain reorganizations, see part II of this subchapter.

(b) *Base period.* As used in this subchapter the term "base period" means the period beginning January 1, 1946, and ending December 31, 1949, except that in the case of a taxpayer whose first taxable year under this subchapter was preceded by a taxable year which ended after December 31, 1949, and before April 1, 1950, and which began before January 1, 1950, the term "base period" means the period of 48 consecutive months ending with the close of such preceding taxable year.

(c) *Average base period net income—determination.* For the purposes of this section the average base period net income of the taxpayer shall be the amount determined under subsection (d), subject to the exception that if the taxpayer is entitled to the benefits of subsection (e) of this section, or section 442, 443, 444, 445, or 446, then the average base period net income shall be the amount determined under subsection (d) or (e) or under such section, whichever results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed.

(d) *Average base period net income—General average.* The average base period net income determined under this subsection shall be determined as follows:

(1) By computing the excess profits net income for each month in the base period. The excess profits net income for any month during any part of which the taxpayer was in existence shall be the excess profits net income for the taxable year in which such month falls divided by the number of full calendar months in such year, but in no case shall the excess profits net income for any month be less than zero. The excess profits net income for any month during no part of which the taxpayer was in existence shall be zero.

(2) By eliminating from the base period whichever of the following twelve months results in the higher average base period net income—

(A) The twelve consecutive months the elimination of which produces the highest average base period net income, or

(B) The twelve months which remain after retaining in the base period the thirty-six consecutive months which produce the highest average base period net income.

(3) By computing the aggregate of the excess profits net income for each of the thirty-six months remaining in the base period.

(4) By dividing by 3 the amount ascertained under paragraph (3).

(e) *Average base period net income—alternative based on growth*—(1) *Taxpayers to which subsection applies.* A taxpayer shall be entitled to the benefits of this subsection if the taxpayer commenced business before the beginning of its base period, and if either—

(A) (i) The total assets of the taxpayer as of the first day of its base period (when added to the total assets for such day of all corporations with which the taxpayer has the privilege under section 141 of filing a consolidated return for its first taxable year under this subchapter, determined under paragraph (3), did not exceed $20,000,000, and

(ii) The total payroll of the taxpayer (as determined under paragraph (4)) for the last half of its base period is 130 per centum or more of its total payroll for the first half of its base period, or the gross receipts of the taxpayer (as determined under paragraph (5) for the last half of its base period is 150 percentum or more of its gross receipts for the first half of its base period; or

(B) (i) The taxpayer's net sales for the period beginning January 1, 1950, and ending June 30, 1950, when multiplied by 2, equals or exceeds 150 per centum of its average net sales for the calendar years 1946-1947; and

(ii) 40 per centum or more of the taxpayer's net sales for the calendar year 1950 is attributable to a product, or class of products (including any article in which such product or class of products is the principal component and including any article which is a component of such product or class of products), of a kind not generally available to the public at any time prior to January 1, 1946, and

(iii) The amount of the taxpayer's net sales which is attributable to such product or class of similar products, for the calendar year 1946 is 5 per centum or less of the amount of its net sales so attributable for the calendar year 1949. For the purposes of this subparagraph, the term "net sales" with respect to any period means the total amount received or accrued during such period from the sale, exchange, or other disposition of stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business; reduced by the amount

of discounts, returns, and allowances paid or incurred for such period.

(2) *Computation.* The average base period net income determined under this subsection shall be determined as follows:

(A) By computing (in the manner provided by the second sentence of subsection (d) (1) the excess profits net income for each of the last 24 months in the base period.

(B) By computing the aggregate of the excess profits net income for each such month.

(C) By dividing by 2 the amount ascertained under subparagraph (B).

(D) By computing the aggregate of the excess profits net income for each of the last twelve months in the base period.

(E) By computing (in the manner provided by the second sentence of subsection (d) (1) the excess profits net income for each of the twelve months in the period beginning July 1, 1949, and ending June 30, 1950. For the purposes of this subparagraph and subparagraph (G) the excess profits net income for any month after December 1949 shall be the "weighted excess profits net income" for the taxable year in which such month falls divided by the number of full calendar months in such year, but in no case shall such excess profits net income for any month be less than zero. The "weighted excess profits net income" for any taxable year beginning before July 1, 1950, shall be—

(i) 100 per centum of the excess profits net income for the taxable year if such year ends before July 1, 1950;

(ii) 90 per centum of the excess profits net income for the taxable year if such year ends after June 30, 1950, and before October 1, 1950;

(iii) 80 per centum of the excess profits net income for the taxable year if such year ends after September 30, 1950, and before April 1, 1951; and

(iv) 70 per centum of the excess profits net income for the taxable year if such year ends after March 31, 1951.

(F) By computing the aggregate of the excess profits net income for each of the twelve months referred to in subparagraph (E).

(G) In the case of a taxpayer who is entitled to the benefits of this subsection only under paragraph (1) (B) and whose excess profits net income for the calendar year 1949 is not more than 25 per centum of its excess profits net income for the calendar year 1948, by computing—

(i) In the manner provided by subparagraph (E), the excess profits net income for each of the six months in the period beginning July 1, 1948, and ending December 31, 1948, and for each of the six months in the period beginning January 1, 1950, and June 30, 1950, and

(ii) The aggregate of the excess profits net income for each of the twelve months referred to in clause (i).

The average base period net income determined under this subsection shall be the amount ascertained under subparagraph (C), (D), or (F), whichever is the highest, except that in the case of a taxpayer described in subparagraph (G), its average base period net income determined under this subsection shall be the amount ascertained under subparagraph (C), (D), (F), or (G) (ii), whichever is the highest.

(3) *Total assets.* For the purposes of this subsection the taxpayer's total assets as of any day shall be determined as of the beginning of such day and shall be an amount equal to the sum of the cash and the property other than cash, held by such taxpayer for the purposes of the business. Such property shall be included in an amount equal to its adjusted basis for determining gain upon sale or exchange. In case the taxpayer has the privilege under section 141 of filing a consolidated return for its first taxable year under this subchapter, the total assets of the affiliated group as of any day shall be determined under regulations prescribed by the Secretary.

(4) *Total payroll.* As used in this subsection the term "total payroll" with respect to any period means the sum of the salaries, wages, commissions, and other compensation paid or incurred by the taxpayer during such period for personal services actually rendered by employees, excluding the amount thereof which is allowable as a deduction under section 23 (p) and excluding any compensation paid in any medium other than cash. In the event that a taxable year falls partly within such period, there shall be allocated, for the purposes of this paragraph, to the portion of the year within such period an amount of the salaries, wages, commissions, and other compensation for such year in the same proportion as the number of months in such year within the period bears to the total number of months in such year.

(5) *Gross receipts.* As used in this subsection the term "gross receipts" with respect to any period means the sum of:

(A) The total amount received or accrued during such period from the sale, exchange, or other disposition of stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business, and

(B) The gross income, attributable to a trade or business regularly carried on by the taxpayer, received or accrued during such period excluding therefrom—

(i) Gross income derived from the sale, exchange, or other disposition of property;

(ii) Gross income derived from discharge or indebtedness of the taxpayer;

(iii) Dividends on stocks of corporations; and

(iv) Income attributable to recovery of bad debts.

In the event that a taxable year falls partly within such period, there shall be allocated, for the purposes of subparagraphs (A) and (B), to the portion of the year within such period an amount of the total gross receipts (as defined in such subparagraphs) for such year in the same proportion as the number of months in such year within the period bears to the total number of months in such year.

(f) *Capital additions in base period*—(1) *Definition of yearly base period capital.* For the purposes of this subsection, the yearly base period capital for any taxable year shall be the sum of the equity capital (as defined in section 437 (c)) at the beginning of such taxable year and an amount equal to 75 per centum of the daily borrowed capital (as defined in section 439 (b)) for the first day of such taxable year, reduced by the sum of—

(A) The amount of inadmissible assets at the beginning of such taxable year, determined under section 440, minus 25 per centum of the excess, if any, of such amount over the amount of the equity capital (as defined in section 437 (c)) at the beginning of such taxable year.

(B) 75 per centum of the amount of loans to members of a controlled group, determined under paragraph (4), and

(C) 75 per centum of the amount of the adjustment for interest on borrowed capital, determined under paragraph (5).

(2) *Computation of base period capital addition—General Rule.* The amount of the base period capital addition referred to in subsection (a) (1) (B) shall, except in cases otherwise provided for in paragraph (3), be determined as follows:

(A) By computing the yearly base period capital for each of the following years:

(i) The first taxable year of the taxpayer under this subchapter;

(ii) The immediately preceding taxable year; and

(iii) The second preceding taxable year.

(B) By computing the amount of the excess, if any, of the amount ascertained under subparagraph (A) (i) over the higher of the amounts ascertained under subparagraphs (A) (ii) and (A) (iii).

(C) By computing the amount of the excess, if any, of the lower of the amounts ascertained under subparagraphs (A) (i) and (A) (ii) over the amount ascertained under subparagraph (A) (iii).

(D) By adding to the amount ascertained under subparagraph (B) one-half of the amount ascertained under subparagraph (C).

(3) *Special rules in case of abnormality during base period.* In the event that the average base period net income of the taxpayer is determined under section 442, then—

(A) If its average base period net income is determined under section 442 (d), the base period capital addition shall be zero.

(B) If its average base period net income is determined under section 442 (c) (1) by including a substitute excess profits net income for any part of its first taxable year under this subchapter or for the immediately preceding year, the base period capital addition shall be zero.

(C) If its average base period net income is computed under section 442 (c) (1) by including a substitute excess profits net income for any part of the earlier of the taxpayer's two taxable years immediately preceding its first taxable year under this subchapter, the base period capital addition shall be the excess, if any, of the amount ascertained under paragraph (2) (A) (i) over the amount ascertained under paragraph (2) (A) (ii).

(4) *Loan to members of a controlled group.* If, on the first day of any taxable year, the taxpayer and any one or more other corporations are members of the same controlled group, as defined in subsection (g) (6), the amount referred to in paragraph (1) (B) with respect to such taxable year shall be the amount of the indebtedness of such other corporation (or if more than one, such other corporations) to the taxpayer at the beginning of such day. For the purposes of this paragraph, the term "indebtedness" means indebtedness which constitutes daily borrowed capital, as defined in section 439 (b) (1), of such other corporation for such day.

(5) *Adjustment for interest on borrowed capital.* The adjustment for interest on borrowed capital referred to in paragraph (1) (C) with respect to any taxable year shall be determined as follows:

(A) By multiplying any indebtedness of the taxpayer which constitutes daily borrowed capital (as defined in section 439 (b)) for the first day of such taxable year by the annual rate of interest payable upon such indebtedness during such taxable year.

(B) By aggregating the amounts ascertained under subparagraph (A) with respect to all borrowed capital for such day.

(C) By multiplying the aggregate amount ascertained under subparagraph (B) by 100, and dividing the product by 12.

(6) *Cross reference.* For special rules applicable to this subsection see section 441.

(g) *Net capital addition or reduction*—(1) *Net capital addition.* The net capital addition for the taxable year shall, for the purposes of this section, be the excess, divided by the number of days in the taxable year, of the aggregate of the daily capital addition for each day of the taxable year over the aggregate of the daily capital reduction for each day of the taxable year. If there is an increase in inadmissible assets for the taxable year, determined under paragraph (5), the net capital addition shall be the excess of the amount determined under the preceding sentence over—

(A) Unless subparagraph (B) is applicable, the amount of such increase in inadmissible assets;

(B) If the amount of such increase in inadmissible assets is in excess of the net capital addition determined without regard to this sentence and without regard to paragraph (3) (C), the amount of such increase in inadmissible assets minus 25 per centum of such excess.

(2) *Net capital reduction.* The net capital reduction for the taxable year shall, for the purposes of this section, be the excess, divided by the number of days in the taxable year, of the aggregate of the daily capital reduction for each day of the taxable year over the aggregate of the daily capital addition for each day of the taxable year. If there is a decrease in inadmissible assets for the taxable year, determined under paragraph (5), the net capital reduction shall be the excess of the amount determined under the preceding sentence over—

(A) Unless subparagraph (B) is applicable, the amount of such decrease in inadmissible assets;

(B) If the amount of such decrease in inadmissible assets is in excess of the net capital reduction determined without regard to this sentence and without regard to paragraph (4) (C) and (E), the amount of such decrease in inadmissible assets minus 25 percentum of such excess.

(3) *Daily capital addition.* The daily capital addition for any day of the taxable year shall, for the purposes of this section, be the sum of the following:

(A) The aggregate of the amounts of money and property paid in for stock, or as paid-in surplus, or as a contribution to capital, after the beginning of the taxable year and prior to such day.

(B) The amount, if any, by which the equity capital (as defined in section 437 (c)) at the beginning of the taxable year exceeds the equity capital at the beginning of the taxpayer's first taxable year under this subchapter.

(C) 75 per centum of the amount, if any, by which the average borrowed capital for the taxable year (as defined in section 439 (a)) exceeds the daily borrowed capital for the first day of the taxpayer's first taxable year under this subchapter.

(4) *Daily capital reduction.* The daily capital reduction for any day of the taxable year shall, for the purposes of this section, be the sum of the following:

(A) Distributions to shareholders previously made during such taxable year which are not out of the earnings and profits of such taxable year; and

(B) The amount, if any, by which the amount of the equity capital (as defined in section 437 (c)) at the beginning of the taxpayer's first taxable year under this subchapter exceeds the amount of the equity capital at the beginning of the taxable year; and

(C) 75 per centum of the amount, if any, by which the daily borrowed capital (as determined under section 439 (b)) for the first day of the taxpayer's first taxable year under this subchapter exceeds the average borrowed capital for the taxable year; and

(D) The amount determined under paragraph (6), relating to increase in certain inadmissible assets by a member of a controlled group; and

(E) 75 per centum of the amount determined under paragraph (7), relating to increase in loans to a member of a controlled group.

(5) *Definitions with respect to inadmissible assets.* For the purposes of this subsection—

(A) *Average inadmissible assets for the taxable year.* The average inadmissible assets for any taxable year shall be the total of the daily amounts attributable to the inadmissible assets for such taxable year, determined under section 440 (b), divided by the number of days in such taxable year.

(B) *Original inadmissible assets.* The term "original inadmissible assets" means the total of the inadmissible assets for the first day of the taxpayer's first taxable year under this subchapter, determined under section 440 (b).

(C) Increase in inadmissible assets. The term "increase in inadmissible assets" for any taxable year means the excess of the average inadmissible assets for such taxable year over the original inadmissible assets.

(D) *Decrease in inadmissible assets.* The term "decrease in inadmissible assets" for any taxable year means the excess of the original inadmissible assets over the average inadmissible assets for such year.

(6) *Controlled group.* If, on any day of the taxable year, the taxpayer and any one or more other corporations are members of the same controlled group, the amount added to the daily capital reduction under paragraph (4) (D) shall be whichever of the following amounts is the lesser:

(A) The excess of the aggregate of the adjusted basis (for determining gain upon sale or exchange) of stock in such other corporation (or if more than one, in such other corporations) held by the taxpayer at the beginning of such day over the aggregate of the adjusted basis (for determining gain upon sale or exchange) of stock in such other corporation (or if more than one, in such other corporations) held by the taxpayer at the beginning of its first taxable year under this subchapter; or

(B) The excess of the aggregate of the adjusted basis (for determining gain upon sale or exchange) of inadmissible assets held by the taxpayer at the beginning of such day, over the aggregate of the adjusted basis (for determining gain upon sale or exchange) of inadmissible assets held by the taxpayer at the beginning of its first taxable year under this subchapter.

The increase in inadmissible assets for the taxable year shall, for the purposes of paragraph (1), be determined by reducing the inadmissible assets for such day by the amount by which the daily capital reduction for such day is increased under this paragraph. As used in this paragraph, a controlled group means one or more chains of corporations connected through stock ownership with a common parent corporation if (i) more than 50 per centum of the total combined voting power of all classes of stock entitled to vote, or more than 50 per centum of the total value of shares of all classes of stock of each of the corporations (except the common parent corporation) is owned directly by one or more of the other corporations and (ii) the common parent corporation owns directly more than 50 per centum of the total combined voting power of all classes of stock entitled to vote, or more than 50 per centum of the total value of shares of all classes of stock, of at least one of the other corporations.

(7) *Loans to members of a controlled group.* If, on any day of the taxable year, the taxpayer and any one or more other corporations are members of the same controlled group, as defined in paragraph (6), the amount referred to in paragraph (4) (E) shall be the excess of the amount of the indebtedness of such other corporation (or if more than one, such other corporations) to the taxpayer at the beginning of such day over the amount of the indebtedness by such other corporation (or if more than one, such other corporations) to the taxpayer at the beginning of its first taxable year under this subchapter. For the purposes of this paragraph, the term "indebtedness" means indebtedness which constitutes daily borrowed capital, as defined in section 439 (b) (1), of such other corporation for such day.

(8) *Cross reference.* For special rules applicable to this subsection see section 441.

§ 40.435-1 *Excess profits credit based on income; determination of average base period net income*—(a) *Introductory.* In order for a corporation to determine for any particular taxable year the amount of its excess profits credit based on income, it is necessary first to compute the amount of the average base period net income, 85 percent of which is the starting point for computing the excess profits credit based on income. Two methods are provided in section 435 for determining the average base period net income: (1) The general average method, set forth in section 435 (d) and in paragraph (d) of this section, and (2) the alternative method set forth in section 435 (e) applicable to certain taxpayers whose growth entitles them to the benefits of a method provided in such section, if such method results in a lesser excess profits tax.

(b) *Base period.* The term "base period" means the period beginning January 1, 1946, and ending December 31, 1949, except in the case of a taxpayer whose first taxable year ending after June 30, 1950, was preceded by a taxable year which began before January 1, 1950, and ended January 31, February 28, or March 31, 1950. In the latter case the term "base period" means the 48 consecutive months ending with the close of January, February, or March, 1950, as the case may be. A fiscal year taxpayer whose first taxable year ending after June 30, 1950, was preceded by a taxable year which began before January 1, 1950, and ended after March 31, 1950, will use as its base period the period beginning January 1, 1946, and ending December 31, 1949.

(c) *Average base period net income; determination.* The average base period net income is the amount determined under section 435 (d) (for computation, see paragraph (d) of this section), unless the taxpayer is entitled to the benefits of section 435 (e), 442, 443, 444, 445, or 446, in which case the average base period net income shall be the amount determined under whichever section, applicable to the taxpayer, results in the lowest excess profits tax for the taxable year.

(d) *Computation under general average method.* The following steps are required for the computation of the average base period net income under the general average method:

(1) The excess profits net income is determined for each month during which the taxpayer was in existence during the base period. This amount is determined for any month during any part of which the taxpayer was in existence by dividing the excess profits net income (computed in accordance with the provisions of section 433 (b) for the taxable year in which such month falls by the number of full calendar months in such taxable year. In no case shall the excess profits net income for any month be less than zero. The excess profits net income for any month during no part of which the taxpayer was in existence shall be zero.

(2) The 36 months which produce the highest aggregate excess profits net income are selected under either of two methods: (i) The 12 consecutive months having the lowest aggregate excess profits net income may be eliminated; or (ii) the 36 consecutive months having the

highest aggregate excess profits net income may be retained.

(3) The excess profits net income for each of the 36 months selected under subparagraph (2) of this paragraph is aggregated.

(4) The aggregate amount computed under subparagraph (3) of this paragraph is divided by 3.

§ 40.435–2 *Average base period net income; alternative based on growth.* Section 435 (e) provides alternative methods of computing the average base period net income of certain taxpayers whose growth during the base period is shown by increased gross receipts or payroll during the last half of the base period. These alternative methods are also available in certain cases to a taxpayer meeting certain tests with respect to sales of products not generally available prior to 1946.

§ 40.435–3 *Definitions.* For the purpose of section 435 (e)—

(a) *Total assets.* The term "total assets" means an amount equal to the sum of cash and property other than cash, held by the taxpayer for purposes of the business. The total assets as of any day shall be determined as of the beginning of such day. The property is to be included in an amount equal to its adjusted basis for determining gain upon sale or exchange. See, in general, section 113 and the regulations prescribed thereunder. For special rule in the case of certain intangible property, see section 441 (i). If the taxpayer is a member of an affiliated group of corporations which has the privilege under section 141 of filing a consolidated return for its first taxable year ending after June 30, 1950, there shall also be included the total assets of each member of such affiliated group whether or not a consolidated return is filed, and whether or not such corporation was a member of an affiliated group including the taxpayer on the day as of which total assets are computed. Such total assets shall be determined in a manner consistent with the principles applicable with respect to consolidated returns.

(b) *Total payroll.* The term "total payroll" with respect to any period includes all salaries, wages, commissions, and other compensation paid or incurred during such period by the taxpayer for personal services actually rendered by employees. However, there is excluded from the total payroll, the amount thereof which is allowable as a deduction under section 23 (p). There is also excluded any compensation paid in any medium other than cash.

(c) *Gross receipts.* The term "gross receipts" with respect to any period means the sum of: (1) The total amount received or accrued during such period from the sale, exchange, or other disposition of stock in trade of the taxpayer, or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business, and (2) the gross income attributable to a trade or business regularly carried on by the taxpayer, received or accrued during such period, but excluding therefrom—

(i) Gross income derived from the sale, exchange, or other disposition of property;

(ii) Gross income derived from discharge of the taxpayer's indebtedness;

(iii) Dividends on stocks of corporations; and

(iv) Income attributable to recovery of bad debts.

(d) *Net sales.* The term "net sales" with respect to any period means the total amount received or accrued during such period from the sale, exchange, or other disposition of stock in trade of the taxpayer, or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business; reduced by the amount of discounts, returns, and allowances paid or incurred for such period.

(e) *Products not generally available prior to 1946.* For the purpose of section 435 (e) (1) (B), "products not generally available prior to 1946" means a product, or class of products (including any article in which such product or class of products is the principal component and including any article which is a component of such product or class of products) of a kind not generally available to the public at any time prior to January 1, 1946. A product which is a modification of an old product, such as an improvement or change in style, is not a product of the type referred to. A product which was generally available prior to 1946, although not available at all times prior thereto, is also not covered.

§ 40.435–4 *Qualifications for computation of alternative average base period net income based on growth*—(a) *In general.* Section 435 (e) is applicable only to a taxpayer which commenced business before the beginning of its base period and which establishes that it qualifies under either paragraphs (b) or (c) of this section. A taxpayer computing its average base period net income by using an alternative based on growth shall submit with its return a full and complete statement showing the basis upon which each requirement of section 435 (e) is satisfied and all the facts upon which the taxpayer relies.

(b) *Eligibility requirements; general rule.* A taxpayer which commenced business before the beginning of its base period shall be entitled to the benefits of section 435 (e) if its total assets as of the beginning of the first day of its base period did not exceed $20,000,000 and either—

(1) The taxpayer's total payroll for the last half (the last 24 months) of its base period is at least 30 percent greater than the taxpayer's total payroll for the first half (the first 24 months) of its base period, or

(2) The taxpayer's gross receipts for the last half (the last 24 months) of its base period are at least 50 percent greater than the taxpayer's gross receipts for the first half (the first 24 months) of its base period.

Where a taxable year falls partly within the first or second half of the base period, the amounts of the gross receipts or total payroll shall be allocated on a monthly basis to the appropriate period.

(c) *Eligibility requirements; products not generally available prior to 1946.* Regardless of the amount of its total assets as of the beginning of the first day of its base period, a taxpayer which commenced business before the beginning of its base period may compute its average base period net income under section 435 (e) if—

(1) The taxpayer's net sales for the period beginning January 1, 1950, and ending June 30, 1950, when multiplied by 2 is at least 50 percent greater than its average net sales for the calendar years 1946 and 1947, and

(2) At least 40 percent of the taxpayer's net sales for the calendar year 1950 is attributable to products not generally available prior to 1946, and

(3) The amount of the taxpayer's net sales attributable to such products for the calendar year 1946 does not constitute more than 5 percent of the amount of its net sales so attributable for the calendar year 1949.

In order to determine qualification under this subsection, a taxpayer must compute its net sales for each particular period specified. It may not, for example, determine its net sales for a particular specified period by allocating to such period a pro rata portion of net sales for its taxable year which includes such period.

§ 40.435–5 *Computation of average base period net income based on growth*—(a) *Computation.* The following steps are required for the computation of average base period net income under the methods set forth in section 435 (e):

(1) The excess profits net income for each of the last 24 months in the base period is determined as provided in the second sentence of section 435 (d) (1).

(2) The amounts determined under subparagraph (1) of this paragraph are aggregated.

(3) The aggregate amount ascertained under subparagraph (2) of this paragraph is divided by 2.

(4) The excess profits net income for each of the last 12 months in the base period is aggregated.

(5) The excess profits net income (determined as provided in the second sentence of section 435 (d) (1)) or the weighted excess profits net income (as defined in paragraph (b) of this section), as the case may be, for each of the 12 months in the period beginning July 1, 1949, and ending June 30, 1950, is computed.

(6) The amounts determined under subparagraph (5) of this paragraph are aggregated.

(7) If a taxpayer meets the eligibility requirements with respect to products not generally available prior to 1946 (see § 40.435–4 (c)) and does not qualify under the general requirements for the alternative based on growth (see § 40.435–4 (b)), and if its excess profits net income for the calendar year 1949 is not more than 25 percent of its excess profits

net income for the calendar year 1948, then—

(i) The excess profits net income for each of the six months in the period beginning July 1, 1948, and ending December 31, 1948, and the weighted excess profits net income for each of the six months in the period beginning January 1, 1950, and ending June 30, 1950, are computed.

(ii) The amounts determined under subdivision (i) of this subparagraph are aggregated.

(8) The average base period net income under section 435 (e) is the amount ascertained under subparagraphs (3), (4), or (6) of this paragraph, whichever is the highest. In the case of a taxpayer described in subparagraph (7) of this paragraph, the average base period net income is the amount ascertained under subparagraphs (3), (4), (6), or (7) of this paragraph, whichever is the highest.

(b) *Weighted excess profits net income.* For the purpose of paragraph (a) (5) and (7) of this section, the term "weighted excess profits net income" applies to any month after December 1949, and means the weighted excess profits net income for the taxable year in which such month falls, divided by the number of full calendar months in such year. The term "weighted excess profits net income for the taxable year" applies only to taxable years beginning before July 1, 1950 (and ending after December 31, 1949), and is an amount equal to the following percentages of the excess profits net income for such taxable years:

(1) 100 percent of the excess profits net income for the taxable year if such year ends before July 1, 1950;

(2) 90 percent of the excess profits net income for the taxable year if such year ends after June 30, 1950, and before October 1, 1950;

(3) 80 percent of the excess profits net income for the taxable year if such year ends after September 30, 1950, and before April 1, 1951; and

(4) 70 percent of the excess profits net income for the taxable year if such year ends after March 31, 1951.

§ 40.435–6 *Capital additions in base period*—(a) *In general.* (1) If the average base period net income of the taxpayer is determined under the general average method (see § 435 (d) and § 40.435–1 (d)), the excess profits credit of the taxpayer computed under section 435 (a) shall include 12 percent of the amount of the base period capital addition. See section 435 (a) (1) (B). The base period capital addition shall also be available, subject to certain limitations to a corporation computing its average base period net income under section 442, relating to abnormalities during the base period. See section 435 (f) (3) and (d) of this section. No base period capital addition shall be allowed if the average base period net income is computed under the method provided in sections 435 (e), 443, 444, 445, or 446. In the case of installment basis taxpayers and taxpayers with income from long-term contracts, electing under section 455, see section 441 (h).

(2) The base period capital addition is based upon the net addition to capital for the taxpayer's last two taxable years ending before July 1, 1950. Only one-half the net addition to capital for the earlier taxable year is in general taken into account. In determining the net addition to capital, the full increase in equity capital and 75 percent of the increase in borrowed capital are taken into account, subject to adjustments for interest on borrowed capital, for inadmissible assets, and for loans to members of a controlled group of which the taxpayer is a member. The base period capital addition shall in no case be less than zero and there is no corresponding downward adjustment to reflect a decrease in capital prior to the first excess profits tax taxable year.

(3) No base period capital addition is permitted or required in the case of a foreign corporation.

(4) For special rules applicable in the case of a corporation a party to a transaction described in section 461 (a), see section 464, and for rules applicable in general to this section, see section 441.

(b) *Yearly base period capital*—(1) *Definition.* The first step in the computation of the base period capital addition under section 435 (f) is the determination of the yearly base period capital for the taxpayer's first taxable year ending after June 30, 1950, and for each of the two preceding taxable years. For the purposes of section 435 (f), the yearly base period capital for any taxable year shall be the sum of the equity capital, as defined in section 437 (c), at the beginning of the first day of such taxable year, plus an amount equal to 75 percent of the daily borrowed capital, as defined in section 439 (b), for the first day of such taxable year. Such sum shall be reduced by the sum of:

(i) The amount of the inadmissible assets held by the taxpayer at the beginning of such taxable year, determined under section 440, minus 25 percent of the excess, if any, of such amount over the amount of the equity capital (as defined in section 437 (c)) at the beginning of the first day of such taxable year;

(ii) 75 percent of the amount of loans to members of a controlled group; and

(iii) 75 percent of the amount of the adjustment for interest on borrowed capital.

(2) *Equity capital.* The equity capital at the beginning of the first day of any taxable year shall be determined under section 437 (c) and under the provisions of law, such as section 441 and section 470, applicable to determinations under section 437 (c). See § 40.437–5.

(3) *Borrowed capital.* The amount of the daily borrowed capital, 75 percent of which is added to the equity capital, shall be determined under section 439 (b) as of the beginning of the first day of each taxable year. See § 40.439–1.

(4) *Inadmissible assets.* The amount of the inadmissible assets held by the taxpayer as of the beginning of the first day of each taxable year constitutes a reduction, under section 435 (f) (1) (A), in the computation of the yearly base period capital for such taxable year. The amount of the inadmissible assets shall be determined under section 440. See § 40.440–1. Where the amount of the inadmissible assets at the beginning of any taxable year is in excess of the equity capital at such time, the amount of inadmissible assets, for the purposes of determining the reduction under section 435 (f) (1) (A), is reduced by 25 percent of such excess.

(5) *Loans to members of a controlled group.* If on the first day of any taxable year the taxpayer was a member of a controlled group, 75 percent of the amount of the indebtedness to the taxpayer, as of the beginning of such day, of any other members of the controlled group constitutes a reduction, under section 435 (f) (1) (B), in computing the yearly base period capital for such taxable year. For this purpose, the term "indebtedness" means indebtedness which constitutes daily borrowed capital, as defined in section 439 (b) (1), of such other member of the controlled group for such day. For definition of controlled group, see section 435 (g) (6).

(6) *Adjustment for interest on borrowed capital.* In computing the yearly base period capital for any taxable year, section 435 (f) (1) (C) requires that such amount shall be reduced by 75 percent of the amount of the adjustment computed under section 435 (f) (5) for interest on indebtedness of the taxpayer which constitutes daily borrowed capital. The computation of the adjustment for interest on borrowed capital under section 435 (f) (5) and of the reduction under section 435 (f) (1) (C) is illustrated by the following example:

*Example.* The Y corporation, which makes its return on the calendar year basis, has daily borrowed capital on January 1, 1948, in the following amounts: $100,000 of 4 percent bonds, maturing January 31, 1948, $50,000 of 6 percent notes maturing August 31, 1949, and $40,000 of 5 percent bonds maturing December 31, 1955, which indebtedness constitutes the total amount of its daily borrowed capital, as defined in section 439 (b), as of the beginning of such day. The adjustment for interest on borrowed capital is $75,000 and the reduction for such adjustment is $56,250, computed as follows:

| | |
|---|---|
| (1) $100,000 multiplied by 4 percent | $4,000 |
| (2) $50,000 multiplied by 6 percent | 3,000 |
| (3) $40,000 multiplied by 5 percent | 2,000 |
| (4) Aggregate of items (1), (2), and (3) | 9,000 |
| (5) Item (4) multiplied by 100 | 900,000 |
| (6) Adjustment for interest on borrowed capital (item (5) divided by 12) | 75,000 |
| (7) Reduction required by section 435 (f) (1) (C) (75 percent of item 6) | 56,250 |

(c) *Computation of base period capital addition; general rule.* (1) The computation of the base period capital addition is based on a comparison of the yearly base period capital, as determined under section 435 (f) (1) and under paragraph (b) of this section, for each of three taxable years: (i) The taxpayer's first taxable year ending after June 30, 1950, (ii) the taxpayer's immediately preceding taxable year, and (iii) the taxpayer's second preceding taxable year.

(2) The amount of the base period capital addition shall be determined as follows:

(i) By computing the amount of the excess, if any, of the amount of the yearly base period capital for the taxpayer's first taxable year ending after June 30, 1950, over the higher of (*a*) the amount of the yearly base period capital for the first preceding taxable year, or (*b*) the amount of the yearly base period capital for the second preceding taxable year.

(ii) By computing the amount of the excess, if any, of the lower of (*a*) the amount of the yearly base period capital for the taxpayer's first taxable year ending after June 30, 1950, or (*b*) the amount of the yearly base period capital for the first preceding taxable year, over the amount of the yearly base period capital for the second preceding taxable year.

(iii) By adding the amount ascertained under subparagraph (1) of this paragraph and one-half of the amount ascertained under this subparagraph. The sum so determined is the base period capital addition of the taxpayer.

(3) *Example.* Corporations X, Y, and Z, which make their returns on the calendar year basis, have yearly base period capital, as determined under section 435 (f) (1), as follows:

| | X | Y | Z |
|---|---|---|---|
| Jan. 1, 1948 | $100,000 | $100,000 | $100,000 |
| Jan. 1, 1949 | 120,000 | 140,000 | 70,000 |
| Jan. 1, 1950 | 140,000 | 110,000 | 130,000 |

The base period capital additions of corporations X, Y, and Z are $30,000, $5,000, and $30,000, respectively, computed as follows:

| | X | Y | Z |
|---|---|---|---|
| (i) Excess of yearly base period capital for 1950 over higher of such amount for 1949 and 1948: | | | |
| (A) Yearly base period capital Jan. 1, 1950 | $140,000 | $110,000 | $130,000 |
| (B) Higher of such amount for 1949 and for 1948 | 120,000 | 140,000 | 100,000 |
| (C) Excess of (A) over (B) | 20,000 | 0 | 30,000 |
| (ii) One-half excess of lower of yearly base period capital for 1950 and 1949 over such amount for 1948: | | | |
| (A) Lower of such amount for 1950 and 1949 | 120,000 | 110,000 | 70,000 |
| (B) Amount for 1948 | 100,000 | 100,000 | 100,000 |
| (C) Excess of (A) over (B) | 20,000 | 10,000 | 0 |
| (D) One-half of (C) | 10,000 | 5,000 | 0 |
| (iii) Base period capital addition (sum of (i) and (ii)) | 30,000 | 5,000 | 30,000 |

(d) *Special rules in case of abnormality during base period.* The base period capital addition, in the case of a taxpayer computing its average base period net income under section 442, is subject to the following rules:

(1) If more than 12 of the 36 months in the period subject to adjustment fall within taxable years the excess profits net income of which was adversely affected by an abnormality, the base period capital addition is zero.

(2) If 12 or fewer of the 36 months in the period subject to adjustment fall within a taxable year or years the excess profits net income of which was adversely affected by an abnormality, and

(i) If a substitute excess profits net income (in excess of 110 percent of excess profits net income) is computed for any part of the taxpayer's first taxable year ending after June 30, 1950, or for any part of the immediately preceding taxable year, the base period capital addition is zero.

(ii) If a substitute excess profits net income (in excess of 110 percent of excess profits net income) is computed for any part of the earlier of the taxpayer's two taxable years immediately preceding its first taxable year ending after June 30, 1950, the base period capital addition shall be the excess, if any, of the amount of the yearly base period capital determined under the rules provided in section 435 (f) (1) and in paragraph (b) of this section for the first taxable year ending after June 30, 1950, over the amount of such yearly base period capital for the immediately preceding taxable year.

(iii) If neither subdivision (i) nor subdivision (ii) of this subparagraph applies, the base period capital addition is determined in accordance with the general rule provided in paragraph (c) of this section.

§ 40.435–7 *Net capital addition or reduction*—(a) *In general.* (1) In addition to adjustments in certain cases for capital changes during the base period (see section 435 (f)), it is also necessary in computing the excess profits credit under section 435 to make adjustments for capital changes occurring after the beginning of the taxpayer's first taxable year ending after June 30, 1950. Section 435 (a) provides that the excess profits credit computed under that section shall be increased or decreased, as the case may be, by 12 percent of the net capital addition or reduction computed under section 435 (g). The net capital addition (or reduction), in general, consists of the net increase (or decrease) in equity and borrowed capital, determined by comparing the equity and borrowed capital for the taxable year with the equity and borrowed capital at the beginning of the first day of the taxpayer's first taxable year ending after June 30, 1950. For this purpose borrowed capital is taken into account at 75 percent. Under certain circumstances an adjustment is made with respect to inadmissible assets and loans to members of a controlled group of corporations of which the taxpayer is a member.

(2) For rules applicable if the average base period net income is computed under the provisions of section 443, relating to change in products or services, see § 40.443–3 (b). For rules applicable if the average base period net income is computed under the provisions of section 445, relating to new corporations, see § 40.445–2 (c). For rules applicable in the case of installment basis taxpayers and taxpayers with income from long-term contracts, electing under section 455, see section 441 (h).

(3) No net capital addition or reduction is permitted or required in the case of a foreign corporation.

(4) For special rules applicable in the case of a corporation a party to a transaction described in section 461 (a), see section 463. See also section 441 for additional rules generally applicable to this section.

(5) In order to determine the net capital addition or reduction, it is necessary to determine the daily capital addition and reduction for each day of the taxable year. The items which shall be taken into account in computing the daily capital addition and the daily capital reduction for each day are described in paragraphs (b) and (c) of this section.

(b) *Daily capital addition.* The daily capital addition for any day of the taxable year is the sum of the following amounts:

(1) The aggregate of the amounts of money and property paid-in in good faith for purposes of the business for stock, or as paid-in surplus, or as a contribution to capital, after the beginning of the taxable year and prior to such day. For rules for determination of the amount so paid in, see section 441.

(2) The amount, if any, by which the equity capital (as defined in section 437 (c)) at the beginning of the taxable year exceeds the equity capital at the beginning of the taxpayer's first taxable year ending after June 30, 1950. The amount of the equity capital shall be determined as of the beginning of the first day of each such taxable year. For rules governing the computation of the amount of equity capital, see sections 437 (c), 441, and 470, and the regulations under such sections.

(3) 75 percent of the excess, if any, of the average borrowed capital for the taxable year (as determined under section 439 (a)) over the daily borrowed capital (as defined in section 439 (b)) for the first day of the taxpayer's first taxable year ending after June 30, 1950. See § 40.439–1.

(c) *Daily capital reduction.* The daily capital reduction for any day of the taxable year is the sum of the following amounts:

(1) The aggregate of the amounts of distributions to shareholders previously made during the taxable year which are not out of the earnings and profits of such taxable year. For each day of the taxable year, the daily amount of distributions not out of earnings and profits of such year is the total amount of such distributions made during the year and prior to such day. For rules for determination of distributions, see section 441.

(2) The amount, if any, by which the amount of the equity capital (as defined in section 437 (c)) at the beginning of the taxpayer's first taxable year ending after June 30, 1950, exceeds the amount of the equity capital at the beginning of the taxable year. The amount of the equity capital shall be determined as of the beginning of the first day of each taxable year. See sections 437 (c), 441, and 470, and the regulations under such sections for rules relating to the computation of equity capital.

(3) 75 percent of the amount, if any, by which the daily borrowed capital (as determined under section 439 (b)) for

the first day of the taxpayer's first taxable year ending after June 30, 1950, exceeds the average borrowed capital for the taxable year (as defined in section 439 (a)).

(4) The amount determined under section 435 (g) (6), relating to an increase in certain inadmissible assets held by the taxpayer, if the taxpayer and one or more other corporations are members of a controlled group of corporations. Section 435 (g) (6) defines controlled group. The amount to be included in the daily capital reduction for any day, with respect to such increase, shall be the amount determined under subdivisions (i) or (ii) of this subparagraph, whichever is the lesser:

(i) The excess of the aggregate of the adjusted basis (for determining gain upon sale or exchange) of stock in such other corporation (or if more than one, in such other corporations) held by the taxpayer at the beginning of such day over the aggregate of the adjusted basis (for determining gain upon sale or exchange) of stock in such other corporation (or if more than one, in such other corporations) held by the taxpayer at the beginning of its first taxable year ending after June 30, 1950.

(ii) The excess of the aggregate of the adjusted basis (for determining gain upon sale or exchange) of inadmissible assets held by the taxpayer at the beginning of such day over the aggregate of the adjusted basis (for determining gain upon sale or exchange) of inadmissible assets held by the taxpayer at the beginning of its first taxable year ending after June 30, 1950.

(5) 75 percent of the amount determined under section 435 (g) (7), relating to any increase in loans to a member of a controlled group of corporations of which the taxpayer is a member. The daily amount of any increase in loans to a member of a controlled group for any day of the taxable year shall be the excess of the amount of the indebtedness (as defined in section 439 (b) (1)) of such other corporation (or if more than one, such other corporations) to the taxpayer at the beginning of such day over the amount of the indebtedness of such other corporation (or if more than one, such other corporations) to the taxpayer at the beginning of the taxpayer's first taxable year ending after June 30, 1950.

(d) *Computation of net capital addition.* (1) The net capital addition for the taxable year is the excess, divided by the number of days in the taxable year, of the aggregate of the daily capital addition for each day of the taxable year over the aggregate of the daily capital reduction for each day of the taxable year. This amount is to be reduced where there is an increase in inadmissible assets (as defined in section 440 (a)) for the taxable year. For the determination of the amount attributable to inadmissible assets for any day, see section 440 (b). Where the total of the daily amounts attributable to inadmissible assets for the taxable year, divided by the number of days in the taxable year, exceeds the total of the inadmissible assets for the first day of the taxpayer's first taxable year ending after June 30, 1950, there is an increase in inadmissible assets for the taxable year. The net capital addition shall be reduced by the amount of such increase. However, certain adjustments to such increase in inadmissible assets must be made in the following cases:

(i) Where there is a daily capital reduction for any day of the taxable year under section 435 (g) (4) (D), the increase in inadmissible assets shall be determined by reducing the inadmissible assets for such day by the amount by which the daily capital reduction for such day is increased under section 435 (g) (4) (D).

(ii) If the amount of the increase in inadmissible assets, as adjusted under subdivision (i) of this subparagraph, is in excess of the net capital addition computed without regard to section 435 (g) (3) (C), relating to increase in borrowed capital, then such increase in inadmissible assets shall be further reduced. The amount of such reduction shall be an amount equal to 25 percent of the excess described in the preceding sentence.

The net capital addition for the taxable year shall in no case be reduced below zero by an increase in inadmissible assets.

(2) For the purpose of section 435 (g) (1), the amount of inadmissible assets for any day shall be determined as provided in section 440 (b). The ratio of such assets to total assets provided in section 440 (b) is not applicable in computing the excess profits credit under section 435.

(e) *Computation of net capital reduction.* (1) The net capital reduction for the taxable year is the excess, divided by the number of days in the taxable year, of the aggregate of the daily capital reduction for each day of the taxable year over the aggregate of the daily capital addition for each day of the taxable year. This amount shall be reduced where there is a decrease in inadmissible assets (as defined in section 440 (a)) for the taxable year. For the determination of the amount attributable to inadmissible assets for any day, see section 440 (b). Where the total of the inadmissible assets for the first day of the taxpayer's first taxable year ending after June 30, 1950, exceeds the total of the daily amounts attributable to the inadmissible assets for the taxable year, divided by the number of days in such year, there is a decrease in inadmissible assets for the taxable year. The amount of the net capital reduction is to be reduced by the amount of such decrease. However, if the amount of such decrease in admissible assets is in excess of the net capital reduction computed without regard to section 435 (g) (4) (C) and (E), relating to a decrease in borrowed capital and an increase in loans to members of a controlled group of corporations of which the taxpayer is a member, then such decrease in inadmissible assets shall be reduced. The amount of such reduction shall be an amount equal to 25 percent of the excess described in the preceding sentence. The net capital reduction for the taxable year shall in no case be reduced below zero as a result of a decrease in inadmissible assets.

(2) For the purpose of section 435 (g) (2), the amount of inadmissible assets for any day shall be determined as provided in section 440 (b). The ratio of such assets to total assets provided in section 440 (b) is not applicable in computing the excess profits credit under section 435.

SEC. 436. EXCESS PROFITS CREDIT—BASED ON INVESTED CAPITAL.

(a) *General rule.* In the case of a domestic corporation (except a corporation described in subsection (b)) the excess profits credit for any taxable year computed under this section shall be the sum of the following:

(1) The invested capital credit computed under section 437, reduced by the amount computed under section 440 (b) (relating to inadmissible assets), and

(2) The new capital credit, if any, computed under section 438 (a).

(b) *Foreign corporations and corporations entitled to benefits of section 251*—(1) *Computation of credit.* In the case of a foreign corporation engaged in a trade or business within the United States, and in the case of a corporation entitled to the benefits of section 251, the excess profits credit for any taxable year computed under this section shall be determined in accordance with rules and regulations prescribed by the Secretary, under which—

(A) *General rule.* The excess profits credit shall be the invested capital credit computed under section 437, reduced by the amount computed under section 440 (b) (relating to inadmissible assets). In computing the invested capital credit for the purposes of this subsection, (i) the invested capital for any taxable year shall (in lieu of the amount provided in section 437 (b) (1)) be the aggregate, divided by the number of days in such year, of the sum of the equity capital (determined under section 437 (c)) as of the beginning of each day of such taxable year and 75 per centum of the daily borrowed capital (determined under section 439 (b)) for each such day, (ii) the term "assets" as used in section 437 (c) shall be considered as referring to United States assets, (iii) the term "liabilities" as used in such section shall be considered as referring to United States liabilities, and (iv) the daily borrowed capital shall be determined under section 439 (b) by reference only to United States liabilities. In the application of section 440, the terms "admissible assets" and "inadmissible assets" shall include only United States assets.

(B) *Exception.* If the Secretary determines that the United States assets of the taxpayer cannot satisfactorily be segregated from its other assets or that the United States liabilities of the taxpayer cannot satisfactorily be segregated from its other liabilities, the invested capital of the taxpayer shall be an amount (in lieu of the amount ascertained under subparagraph (A)) which is the same percentage of the sum of the equity capital of the taxpayer, determined under section 437 (c) as of the end of the last day of the taxable year without the application of this subparagraph, and 75 per centum of the daily borrowed capital determined under section 439 (b) for the day following such last day without the application of this subparagraph, which the net income for the taxable year from sources within the United States is of the total net income of the taxpayer for such year.

(2) *Definitions.* As used in this subsection—

(A) The term "United States assets" means assets held by the taxpayer (in good faith for the purposes of the business) in the United States, determined in accordance with rules and regulations prescribed by the Secretary.

(B) The term "United States liabilities" means the liabilities of the taxpayer which are directly related to its United States assets, determined in accordance with rules and regulations prescribed by the Secretary.

§ 40.436–1 *Excess profits credit based on invested capital; domestic corporations.* Any domestic corporation may compute its excess profits credit under the invested capital method. Such credit, except in the case of a corporation entitled to the benefits of section 251, is an amount equal to the sum of:

(a) The invested capital credit computed under section 437, reduced by the amount computed under section 440 (b), relating to inadmissible assets, and

(b) The new capital credit, if any, computed under section 438 (a).

§ 40.436–2 *Foreign corporations and corporations entitled to benefits of section 251.* In the case of a foreign corporation engaged in trade or business within the United States, and in the case of a corporation entitled to the benefits of section 251 (on account of deriving a large portion of its gross income from sources within possessions of the United States), the excess profits credit for any taxable year computed under this section shall be the invested capital credit provided in section 437, reduced by the amount computed under section 440 (b), relating to inadmissible assets, with the following exceptions:

(a) In lieu of the amount provided in section 437 (b) (1), the invested capital for any taxable year shall be the aggregate, divided by the number of days in such year, of the sum of (1) the equity capital (determined under section 437 (c)) as of the beginning of each day of such taxable year, and (2) 75 percent of the daily borrowed capital (determined under section 439 (b)) for each such day.

(b) For the purpose of determining equity capital for any day under paragraph (a) of this section, the terms "assets" and "liabilities" as used in section 437 (c) shall include only United States assets and liabilities. For the purpose of paragraph (a) of this section the "daily borrowed capital" shall be determined under section 439 (b) by reference only to United States liabilities. In the application of the provisions of section 440 in reduction of the invested capital credit (determined under section 437 as provided in paragraph (a) of this section), the terms "admissible assets" and "inadmissible assets" shall include only United States assets. A corporation described in section 436 (b) may not elect to compute its invested capital under section 458, relating to historical invested capital.

(c) In cases in which the Commissioner determines that the United States assets or liabilities cannot satisfactorily be segregated from the corporation's other assets or liabilities, the invested capital of the corporation shall be (in lieu of the amount determined under paragraph (a) of this section) an amount which is the same percentage of:

(1) The sum of (i) the equity capital determined under section 437 (c) as of the end of the last day of the taxable year and determined without regard to paragraph (b) of this section, and (ii) 75 percent of the daily borrowed capital determined under section 439 (b) as of the beginning of the day following the last day of the taxable year and determined without regard to paragraph (b) of this section, as

(2) The net income for the taxable year from sources within the United States is of the net income of the taxpayer from all sources for such year.

(d) For the purpose of section 436 (b) and of paragraph (b) of this section, the term "United States assets" means assets either (1) employed by the taxpayer in the United States in carrying on its trade or business therein, or (2) of a kind the income from which is income from sources within the United States under section 119 and the regulations prescribed thereunder regardless of where the evidence of the property rights in such assets are held. The term "United States liabilities" means liabilities directly related to the United States assets, such as mortgages or other liens on United States assets and any liabilities attributable to the business conducted in the United States or to the income from sources within the United States.

SEC. 437. INVESTED CAPITAL CREDIT.

(a) *Definition.* The invested capital credit for any taxable year shall be the amount shown in the following table:

| If the invested capital for such year (as defined in subsection (b) (1)) is: | The credit shall be: |
|---|---|
| Not over $5,000,000 | 12% of the invested capital. |
| Over $5,000,000 but not over $10,000,000 | $600,000, plus 10% of the excess over $5,000,000. |
| Over $10,000,000 | $1,100,000, plus 8% of the excess over $10,000,000. |

(b) *Invested capital*—(1) *Election of taxpayer.* The invested capital for any taxable year shall be the adjusted invested capital determined under paragraph (2), except that if the taxpayer elects in its return for such taxable year to compute its invested capital under the provisions of section 458, the invested capital for such year shall be the historical invested capital determined under section 458. For the invested capital of certain insurance companies, see paragraph (3).

(2) *Adjusted invested capital.* The adjusted invested capital for any taxable year (hereinafter in this paragraph referred to as "the taxable year") shall be the sum of—

(A) The equity capital (as defined in subsection (c)) as of the beginning of the taxable year;

(B) The capital addition for the taxable year computed under subsection (d);

(C) 75 per centum of the average borrowed capital for the taxable year computed under section 439 (a); and

(D) The recent loss adjustment computed under subsection (f),

minus the capital reduction for the taxable year computed under subsection (e). If the amount of the adjusted invested capital so computed is over $5,000,000, such amount shall be reduced by the net new capital addition computed under section 438 (b).

(3) *Mutual insurance company (other than life or marine).* The invested capital of a mutual insurance company (other than life or marine) shall be the mean of its surplus, plus 50 per centum of the mean of all reserves required by law, both surplus and reserves being determined at the beginning and end of the taxable year, and it may include as equity capital its organization expenses. The surplus shall include all of the assets of the company other than the reserves required by law.

(c) *Definition of equity capital.* The equity capital of the taxpayer as of any time shall be the total of its assets held at such time in good faith for the purposes of the business, reduced by the total of its liabilities at such time. For such purposes, the amount attributable to each asset shall be determined by ascertaining the adjusted basis thereof (or, in the case of money, the amount thereof) and the adjusted basis shall be the adjusted basis for determining gain upon sale or exchange. In the case of an insurance company (other than mutual and other than life or marine), 50 per centum of its reserves required by law (other than reserves used in computing borrowed capital under section 439 (b) (2)) shall be considered as equity capital and, it may include as equity capital its organization expenses. In the case of a bank (as defined in section 104) its reserves for bad debts shall not be treated as liabilities. In the case of assets subject to a mortgage or other lien, the amount of the indebtedness secured by such mortgage or lien shall be considered as a liability of the taxpayer whether or not the taxpayer assumed or agreed to pay such indebtedness.

(d) *Capital addition for the taxable year.* The capital addition for the taxable year shall be the aggregate of the daily capital addition for each day of the taxable year, divided by the number of days in such year. The daily capital addition for each day of the taxable year shall be the aggregate of the amount of money and property paid in after the beginning of such taxable year and prior to such day for stock, or as paid-in surplus, or as a contribution to capital.

(e) *Capital reduction for the taxable year.* The capital reduction for the taxable year shall be the aggregate of the daily capital reduction for each day of the taxable year, divided by the number of days in such year. The daily capital reduction for each day of the taxable year shall be the amount of the distributions previously made during the taxable year which are not out of the earnings and profits of such taxable year.

(f) *Recent loss adjustment*—(1) *Determination.* The recent loss adjustment for any taxable year shall be the excess of the aggregate of the net operating loss for each taxable year in the recent loss period over the aggregate of the net income for each taxable year in such period. For purposes of this subsection, the term "recent loss period" means whichever of the following periods results in a higher recent loss adjustment—

(A) The base period, or

(B) The period beginning January 1, 1940, and ending December 31, 1949.

(2) *Definitions.* For purposes of this subsection—

(A) *Net operating loss.* The net operating loss for any taxable year means the net operating loss as defined in section 122 (a), determined under the law applicable to such taxable year.

(B) *Net income.* The net income for any taxable year means the net income computed with the exceptions, additions, and limitations provided in section 122 (d) (other than paragraph (6) of section 122 (d)), under the law applicable to such taxable year.

(3) *Special rules*—(A) *Only part of taxable year included in recent loss period.* For purposes of this subsection, the net operating loss or net income for a taxable year

only part of which is within the recent loss period shall be such part of the net operating loss or net income for such taxable year, computed without regard to this subparagraph, as the number of months in such taxable year falling within the recent loss period is of the total number of months in such taxable year. For purposes of this subsection, a fractional part of a month shall be disregarded unless it amounts to more than half a month in which case it shall be considered as a month.

(B) *Recent losses of component corporations.* The recent loss adjustment shall be separately computed for each corporation which is a component corporation of the taxpayer within the meaning of part II of this subchapter, and the amount so computed shall be added to the recent loss adjustment of the taxpayer. For purposes of such computation, the recent loss period of the component corporation shall not include any period after the date of the trasaction in which such corporation became a component corporation of the taxpayer. The recent loss adjustment of the component corporation, for the purpose of computing the adjusted equity capital of any corporation (including the component corporation) other than the taxpayer for a taxable year ending after such date shall be reduced by the amount with respect to such component corporation which, under this subsection, is added to the recent loss adjustment of the taxpayer.

§ 40.437–1 *Invested capital credit.* The invested capital credit is an amount equal to 12 percent of the taxpayer's invested capital for the taxable year, except that if such invested capital for any taxable year exceeds $5,000,000, the credit for such taxable year is an amount determined in accordance with the table set forth in section 437 (a).

§ 40.437–2 *Invested capital*—(a) *Definition.* The "invested capital" of the taxpayer means whichever one of the following amounts the taxpayer is required to use for the purpose of determining its credit based on invested capital:

(1) Adjusted invested capital computed under section 437 (b) (2).

(2) Historical invested capital computed under section 458.

(3) In the case of a mutual insurance company other than life or marine, the invested capital computed under section 437 (b) (3).

(4) In the case of a foreign corporation and in the case of a corporation entitled to the benefits of section 251, the invested capital computed under the rules provided in section 436 (b).

(b) *General rule.* The invested capital of every taxpayer is the adjusted invested capital for the taxable year computed under section 437 (b) (2), unless paragraph (c) or (d) of this section applies to the taxpayer for the taxable year.

(c) *Election to use historical invested capital.* If the taxpayer (other than a taxpayer described in paragraph (d) of this section) elects on its return for the taxable year to compute its invested capital under the provisions of section 458, the invested capital of the taxpayer for such year shall be the historical invested capital determined under section 458. A separate election must be made for each taxable year, and an election once made is irrevocable with respect to the taxable year. A taxpayer making such election may not thereafter compute invested capital for the taxable year under section 437 (b) (2). If the historical method is used on the return in determining the excess profits tax liability, the taxpayer will be deemed to have elected the historical method. A taxpayer which computes its excess profits tax on its return on the basis of a credit other than the invested capital credit may nevertheless elect the historical method for such year, in the event that the invested capital credit should subsequently become significant in the determination of its excess profits tax liability for such year, by attaching to its return for the taxable year a statement electing the historical method.

(d) *Special rules.* For the determination of the invested capital of a mutual insurance company other than life or marine, see § 40.437–4. For the determination of the invested capital of a foreign corporation or of a corporation entitled to the benefits of section 251, see § 40.436–2.

§ 40.437–3 *Adjusted invested capital.* (a) The adjusted invested capital is (1) the sum of—

(i) The equity capital (as defined in section 437 (c) and § 40.437–5) as of the beginning of the first day of the taxable year,

(ii) The capital addition for the taxable year computed under section 437 (d) and § 40.437–6.

(iii) 75 percent of the average amount of borrowed capital for the taxable year computed under section 439 (a) and § 40.439–1, and

(iv) The recent loss adjustment computed under section 437 (f) and § 40.437–8;

minus (2) the capital reduction for the taxable year computed under section 437 (e) and § 40.437–7.

(b) Where the amount of the adjusted invested capital so computed is over $5,000,000, such amount shall be reduced by the net new capital addition, computed under section 438 (b). In such case, a separate credit at the rate of 12 percent is allowed under section 436 (a) (2) and section 438 with respect to such net new capital addition. No computation under section 438 is necessary if the adjusted invested capital does not exceed $5,000,000, since the 12 percent rate is applied to the entire invested capital in such a case.

§ 40.437–4 *Invested capital of mutual insurance companies other than life or marine.* The invested capital of a mutual insurance company other than life or marine shall be determined as provided in section 437 (b) (3). The invested capital of such an insurance company for any taxable year shall be the mean of the surplus, plus 50 percent of the mean of all reserves required by law, both surplus and reserves being determined at the beginning and end of the taxable year. For this purpose surplus means the excess of all the assets of the company over the sum of the liabilities of the company, including in such liabilities the reserves required by law. In determining such excess, all the assets of the company, whether admitted or not admitted, shall be included. "Reserves required by law" include not only reserves required by express statutory provisions but also reserves required by the rules and regulations of State insurance departments when promulgated in the exercise of an appropriate power conferred by statute, but do not include assets required to be held for the ordinary running expenses of the business, such as taxes, salaries, and unpaid brokerage. Only reserves commonly recognized as such in insurance accounting are to be taken into consideration in computing the "reserves required by law." In the case of a fire insurance company the only reserves commonly recognized are the "unearned premiums." In addition, the organization expenses of such mutual insurance companies may be included in equity capital.

§ 40.437–5 *Definition of equity capital.* (a) The equity capital of a taxpayer for any day shall be the total of the assets (determined under paragraph (b) of this section) held by it at the beginning of such day in good faith for the purposes of the business, reduced by the total of its liabilities (determined under paragraph (c) of this section) outstanding at the beginning of such day. The determination of the equity capital under section 437 (c) shall be made generally in accordance with sound accounting principles, and shall be consistent with the proper method of accounting used in determining the taxpayer's net income and with the rules applicable in determining the earnings and profits of the taxpayer. For example, in the case of a taxpayer which makes its return on the basis of cash receipts and disbursements, assets and liabilities do not include accounts receivable which are to be included in income when collected and accounts payable which are to be deducted from income when paid. Ordinarily, the starting point in determining the equity capital of a corporation as of the beginning of the first day of its taxable year is its balance sheet as of the close of the preceding taxable year.

(b) (1) The term "total assets" for any day means the sum of the money, plus the aggregate of the adjusted basis (determined as of the beginning of such day) of the property other than money held by the taxpayer at the beginning of such day in good faith for the purposes of the business. Such adjusted basis for any asset is its adjusted basis for determining gain upon sale or exchange for Federal income tax purposes (see, in general, section 113 and the regulations prescribed thereunder), except that in the case of secret processes and formulas, good will, trade-marks, trade brands, franchises, and other like property, such adjusted basis shall be determined without regard to the value of the property as of March 1, 1913. See section 441 (i). The determination of the total assets of any taxpayer shall conform to the method of accounting employed by such taxpayer in determining net income and to the rules applicable in determining its earnings and profits. Thus, a corporation reporting income from installment sales and using the installment method of accounting shall, unless subject to the

provisions of section 441 (h), treat its installment accounts receivable as having an adjusted basis determined under section 44 (d). Similarly, a corporation using the completed contract method of accounting for income from long-term contracts shall, unless subject to the provisions of section 441 (h), treat only its net investment in uncompleted contracts as the adjusted basis thereof. See sections 441 (h) and 455. Treasury stock purchased for investment and held in good faith for the purposes of the business is included in total assets.

(2) For special rule in the case of improvements by a lessee to properties of a lessor railroad corporation, see section 441 (j).

(3) Under section 441 (e), certain distributions to shareholders made during the first 60 days of the taxable year (other than the first taxable year ending after June 30, 1950) are deemed to have been made on the last day of the preceding taxable year. Accordingly, in any case in which section 441 (e) is applicable, the total assets at the beginning of the first day of the taxable year shall be reduced by the amount of the distributions deemed to have been made on the last day of the preceding taxable year, and the taxpayer's liability for such distributions, if any, outstanding at the beginning of such day shall be appropriately adjusted.

(4) For rules applicable in determining the adjusted basis of assets acquired in an intercorporate liquidation, see section 470.

(5) In the case of an insurance company (other than mutual and other than life or marine), the equity capital shall include 50 percent of its reserves required by law, except the reserve for unearned premiums used in computing borrowed capital under section 439 (b) (2). Such an insurance company shall also include its organization expenses in equity capital.

(c) The term "total liabilities" means all liabilities of the taxpayer, absolute and not contingent, and includes those items which constitute liabilities in the sense of debts or obligations. Also included are liabilities assumed by the taxpayer whether or not in connection with assets held by the taxpayer. In the case of assets held by the taxpayer subject to a mortgage or other lien, the amount of the indebtedness secured by such mortgage or lien shall be considered as a liability of the taxpayer whether or not the taxpayer assumed or agreed to pay such indebtedness. If, in a bona fide business transaction, indebtedness of the taxpayer is assumed by another person or property subject to such a mortgage or other lien is disposed of to another person, such indebtedness ceases to be a liability of the taxpayer. The obligation of the taxpayer on its capital stock is not a liability. The determination of the date upon which a liability is incurred is to be made generally in accordance with sound accounting principles and is subject to the rules applicable in determining the taxpayer's earnings and profits. Thus, in the case of a distribution by a corporation, the liability for such distribution is considered incurred at the beginning of the date set for its payment, except that where no date is set for its payment, it is considered incurred on the date when it is declared. See § 40.441–1. Whether a reserve is treated as a liability is dependent upon the nature of the reserve. The reserve for bad debts under section 23 (k) is included as a liability unless under the taxpayer's method of accounting it is treated as a reduction of total assets. In the case of a bank, as defined in section 104, its reserves for bad debts shall neither reduce assets nor be treated as liabilities. A reserve for depletion or depreciation is properly accounted for in determining the adjusted basis of property. Reserves for contingencies and other reserves which are mere appropriations of surplus are not liabilities.

§ 40.437–6 *Capital addition for the taxable year.* (a) The capital addition for the taxable year shall be the aggregate of the daily capital addition for each day of the taxable year, divided by the number of days in such year. The daily capital addition for each day of the taxable year is the aggregate of the money and property paid in after the beginning of such taxable year and prior to such day for stock, or as paid-in surplus, or as a contribution to capital. Only money and property paid-in in good faith for the purposes of the business shall be included.

(b) Under rules provided in section 441, such property is included in determining the daily capital addition in a manner consistent with its inclusion in equity capital under section 437 (c). The rules provided in section 441 with respect to money and property paid in for stock, or as paid-in surplus, or as a contribution to capital, include the following:

(1) Such property shall be included in determining the daily capital addition in an amount equal to its basis (unadjusted) for determining gain upon sale or exchange. If the basis (unadjusted) of the property is a substituted basis, such basis shall be adjusted, with respect to the period before the property was paid in, by an amount equal to the adjustments proper under section 113 (b) (2). See section 441 (b). For rules regarding value as of March 1, 1913, in the case of certain intangible property, see section 441 (i).

(2) If the basis (unadjusted) of property so paid in is a substituted basis, section 441 (g) (1) provides rules with respect to liabilities involved in the exchange, indebtedness of the taxpayer canceled or released in the exchange, and money and property transferred to the transferor.

(3) If an indebtedness of the taxpayer is canceled or released in exchange for stock, or as paid-in surplus, or as a contribution to capital, the amount paid in shall be considered equal to the amount of the indebtedness. See section 441 (g) (2).

(4) Distributions of the corporation's own stock, or rights to acquire its stock, shall not be regarded as money or property paid in for stock, or as paid-in surplus, or as a contribution to capital, and, therefore, do not constitute a capital addition for the taxable year. See section 441 (d).

§ 40.437–7 *Capital reduction for the taxable year.* (a) The capital reduction for the taxable year is the aggregate of the daily capital reduction for each day of the taxable year, divided by the number of days in such year. The daily capital reduction for each day of the taxable year is the amount of the distributions previously made during the current taxable year which are not out of earnings and profits of such taxable year.

(b) As in the case of the capital addition for the taxable year (see § 40.437–6), rules provided in section 441 are applicable in determining the daily capital reduction. Such rules include the following:

(1) A distribution by a corporation of its stock or rights to acquire its stock shall not be considered as a distribution. See section 441 (d).

(2) In determining whether a distribution is out of the earnings and profits of any taxable year, such earnings and profits shall be computed as of the close of such taxable year without diminution by reason of any distribution made during such taxable year or by reason of any income or excess profits tax imposed for such year, and the determination shall be without regard to the amount of earnings and profits at the time the distribution was made. So much of the distributions to shareholders made during the first 60 days of any taxable year (other than the first taxable year ending after June 30, 1950) as does not exceed the accumulated earnings and profits at the beginning thereof shall be considered to have been made on the last day of the preceding taxable year. See section 441 (e) and (f).

§ 40.437–8 *Recent loss adjustment*—(a) *In general.* The amount of the recent loss adjustment computed under section 437 (f) constitutes an item to be included in computing the adjusted invested capital under section 437 (b) (2). The effect of section 437 (f) is, in general, to offset any reduction, reflected in the amount of equity capital at the beginning of the taxable year, which arose from an excess of net operating losses over net income for the recent loss period.

(b) *Computation.* The recent loss adjustment for any taxable year shall be the excess of the aggregate of the net operating loss for each taxable year in the recent loss period over the aggregate of the net income for each taxable year in such period. For the purpose of the preceding sentence, if only part of a taxable year is included in the recent loss period, the net income or net operating loss for such taxable year shall be the portion of such net income or such net operating loss, as the case may be, which is allocable to the recent loss period. Such allocation shall be made on the basis of the number of months in the taxable year which fall within the recent loss period; for the purpose of such allocation, a fractional part of a month shall be disregarded unless it amounts to more than half a month in which case it shall be considered as a month.

(c) *Definitions.* (1) The term "recent loss period" means either the taxpayer's base period or the period beginning January 1, 1940, and ending December 31, 1949, whichever results in the higher recent loss adjustment.

(2) The net operating loss for any taxable year in the recent loss period shall be determined under section 122 (a) under the law applicable to the year for which the loss was sustained. The net income for any taxable year in the recent loss period shall be recomputed with the exceptions, additions, and limitations provided in section 122 (d), under the law applicable to such taxable year. However, no adjustment shall be made under section 122 (d) (6) for excess profits taxes under the World War II law.

(d) *Recent losses of component corporations.* If the taxpayer is an acquiring corporation as defined in section 461 (a), the recent loss adjustment of each of its component corporations, as defined in section 461 (b), shall be separately determined without regard to any period after the date of the transaction in which such corporation became a component corporation of the taxpayer. The recent loss adjustment so determined for each such component corporation is included in the recent loss adjustment of the taxpayer. However, the amount so made available to the taxpayer is not allowed to the component corporation, or to any other corporation with respect to the component corporation, for any taxable year ending after the date such corporation became a component corporation of the taxpayer; for each such taxable year, an amount equal to the amount included in the taxpayer's recent loss adjustment is excluded from the recent loss adjustment of such component or other corporation. The recent loss period used by the taxpayer must be the same for both the computations relating to its own recent losses and the computations relating to those of its component corporations; it is the period (defined in paragraph (c) (1) of this section) for which the sum of the recent loss adjustments is higher.

SEC. 438. NEW CAPITAL CREDIT CHANGES.

(a) *New capital credit.* The new capital credit for any taxable year shall be 12 per centum of the amount of the net new capital addition for the taxable year, except that the credit provided by this subsection shall not be allowed—

(1) If the invested capital for the taxable year (computed without reduction by the amount of the net new capital addition) is $5,000,000 or less;

(2) If the invested capital for the taxable year is the historical invested capital determined under section 458;

(3) If the taxpayer is a mutual insurance company (other than life or marine).

(b) *Net new capital addition.* The net new capital addition for the taxable year shall be the excess, divided by the number of days in the taxable year, of the aggregate of the daily new capital addition (determined under subsection (c)) for each day of the taxable year over the aggregate of the daily new capital reduction (determined under subsection (d)) for each day of the taxable year. If there is an increase in inadmissible assets for the taxable year, determined under section 435 (g) (5), the net new capital addition shall be the excess of the amount determined under the preceding sentence over—

(1) Unless paragraph (2) is applicable, the amount of such increase in inadmissible assets;

(2) If the amount of such increase in inadmissible assets is in excess of the net new capital addition determined without regard to this sentence and without regard to subsection (c) (3) and subsection (d) (3), the amount of such increase in inadmissible assets minus 25 per centum of such excess.

(c) *Daily new capital dddition.* The daily new capital addition for any day of the taxable year shall, for the purposes of this section, be the sum of the following:

(1) The aggregate of the amounts of money and property (other than excluded equity capital as defined in subsection (e)) paid in for stock, or as paid-in surplus, or as a contribution to capital, after the beginning of such taxable year and prior to such day.

(2) The amount, if any, by which the equity capital at the beginning of the taxable year minus the amount of excluded equity capital (as defined in subsection (e)) paid in before the beginning of the taxable year and after the beginning of the taxpayer's first taxable year under this subchapter exceeds the equity capital at the beginning of such first taxable year.

(3) 75 per centum of the amount, if any, by which the increase in the daily borrowed capital for such day exceeds the increase in the excluded borrowed capital for such day. For the purposes of this paragraph the term "increase in the daily borrowed capital" for such day means the amount by which the daily borrowed capital for such day (as defined in section 439 (b)) exceeds the daily borrowed capital for the first day of the taxpayer's first taxable year under this subchapter, and the term "increase in the excluded borrowed capital" for such day means the amount by which the excluded borrowed capital for such day (as defined in subsection (f)) exceeds the excluded borrowed capital for the first day of the taxpayer's first taxable year under this subchapter.

(d) *Daily new capital reduction.* The daily new capital reduction for any day of the taxable year shall be the sum of the following:

(1) Distributions to shareholders previously made during such taxable year which are not out of the earnings and profits of such taxable year; and

(2) The amount, if any, by which the equity capital at the beginning of the taxpayer's first taxable year under this subchapter plus the total amount of excluded equity capital paid in after the beginning of such first taxable year and before the beginning of the taxable year exceeds the amount of the equity capital at the beginning of the taxable year; and

(3) 75 per centum of the amount, if any, by which the daily borrowed capital (as defined in section 439 (b)) for the first day of the taxpayer's first taxable year under this subchapter exceeds the daily borrowed capital for such day.

(e) *Definition of excluded capital.* The term "excluded equity capital" means the amount of money or property paid in for stock, or as paid-in surplus, or as a contribution to capital, to the taxpayer—

(1) By a corporation in an exchange to which section 112 (b) (3), (4), (5), or (10), or so much of section 112 (c), (d), or (e) as refers to section 112 (b) (3), (4), (5), or (10), is applicable (or would be applicable except for section 371 (g)), or would have been applicable if the term "control" had been defined in section 112 (h) to mean the ownership of stock possessing more than 50 per centum of the total combined voting power of all classes of stock entitled to vote or more than 50 per centum of the total value of shares of all classes of stock.

(2) By a transferor corporation if immediately after such transaction the transferor and the taxpayer are members of the same controlled group. As used in this paragraph, a controlled group means one or more chains of corporations connected through stock ownership with a common parent corporation if (A) more than 50 per centum of the total combined voting power of all classes of stock entitled to vote, or more than 50 per centum of the total value of shares of all classes of stock, of each of the corporations (except the common parent corporation) is owned directly by one or more of the other corporations, and (B) the common parent corporation owns directly more than 50 per centum of the total combined voting power of all classes of stock entitled to vote, or more than 50 per centum of the total value of shares of all classes of stock, of at least one of the other corporations.

(f) *Definition of excluded borrowed capital.* The term "excluded borrowed capital" for any day of any taxable year means so much of the daily borrowed capital for such day as consists of outstanding indebtedness to a member of a controlled group, as defined in subsection (e) (2), which includes the taxpayer.

§ 40.438–1 *New capital credit*—(a) *In general.* (1) Section 438 provides that the new capital credit for any taxable year shall be 12 percent of the amount of the net new capital addition for the taxable year. Section 436 (a) provides that the new capital credit as computed under section 438 is to be added to the invested capital credit computed under section 437 in computing the excess profits credit for the taxable year. The new capital credit provided by section 438 shall not be allowed—

(i) If the invested capital for the taxable year (computed without reduction by the amount of the net new capital addition) is $5,000,000 or less, or

(ii) If the invested capital for the taxable year is the historical invested capital determined under section 458, or

(iii) If the taxpayer is a mutual insurance company (other than life or marine).

(2) The net new capital addition, in general, consists of the net increase in equity and borrowed capital determined by comparing the equity and borrowed capital for the taxable year with the equity and borrowed capital as of the beginning of the taxpayer's first taxable year ending after June 30, 1950. For this purpose borrowed capital is taken into account at 75 percent. Under certain circumstances an adjustment is made with respect to inadmissible assets and for excluded equity capital and excluded borrowed capital. In no event is the net new capital addition less than zero.

(3) In the case of installment basis taxpayers and taxpayers with income from long-term contracts, electing under section 455, see section 441 (h). Section 441 also provides additional rules of general application to the determinations under section 438.

§ 40.438–2 *Determination of daily new capital addition.* (a) In order to determine the net new capital addition, it is necessary to ascertain the amount of the daily new capital addition and reduction for each day of the taxable year. This section describes the items which shall constitute a daily new capital addition. Items which constitute a daily new capi-

tal reduction are described in § 40.438–3. The daily new capital addition for any day of the taxable year is the sum of the amounts described in the following paragraphs of this section.

(b) The daily new capital addition for any day includes the aggregate of the amounts of money and property paid-in in good faith for purposes of the business for stock, or as paid-in surplus, or as a contribution to capital after the beginning of the taxable year and prior to such day, subject, however, to an exception for excluded equity capital as defined in section 438 (e). See paragraphs (c) and (d) of this section. For rules applicable in determining the amount of the money and property so paid-in, see section 441 and section 470.

(c) (1) The exception for excluded equity capital referred to in section 438 (c) (1) and in paragraph (b) of this section excludes from the daily new capital addition the amount of any money or property paid in during a taxable year ending after June 30, 1950, for stock, or as paid-in surplus, or as a contribution to capital, in an exchange to which section 112 (b) (3), (4), (5), or (10), or so much of section 112 (c), (d), or (e) as refers to section 112 (b) (3), (4), (5), or (10), is applicable, or in an exchange to which such provisions of section 112 would be applicable if the control requirement for the purpose of applying those provisions had been defined to mean the ownership of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock. The exception described in the preceding sentence is determined without regard to section 371 (g), relating to certain exchanges under Supplement R of chapter 1 to which the specified provisions of section 112 would also be applicable.

(2) Example: The A Corporation issues stock during its taxable year beginning January 1, 1952, to the B Corporation in exchange for the transfer of certain property by the B Corporation. Immediately after the transfer the stock acquired by the B Corporation has a value of $10,000, the total value of all classes of stock of the A Corporation then outstanding amounting to $18,000. The A Corporation obtains no daily new capital addition, since the property for which the new stock was issued was obtained in an exchange to which section 112 (b) (5) would be applicable if the term "control" had been defined in section 112 (h) so as to include either the ownership of stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of all classes of stock outstanding.

(d) (1) The exception for excluded equity capital referred to in section 438 (c) (1) and in paragraph (b) of this section also excludes from the daily new capital addition any money or property paid in to the taxpayer by a transferor corporation if immediately after such transaction the transferor and the taxpayer are members of the same controlled group as that term is defined in section 438 (e) (2).

(2) Example: The A Corporation owns stock in the B Corporation and the B Corporation owns stock in the C Corporation. The A Corporation transfers property to the C Corporation in exchange for stock of the C Corporation. Immediately after the transfer the stock owned by the A Corporation in the B Corporation possesses more than 50 percent of the total combined voting power of all classes of stock entitled to vote. Also immediately after such transfer the stock owned by the B Corporation in the C Corporation has a value equal to more than 50 percent of the total value of all classes of stock of the C Corporation. The C Corporation obtains no daily new capital addition through the acquisition of the property from the A Corporation in exchange for its stock, since immediately after the transfer the A Corporation, the transferor, and the C Corporation, the transferee, are members of the same controlled group.

(e) The daily new capital addition for any day includes the amount, if any, by which (1) (i) the equity capital at the beginning of the taxable year minus (ii) the amount of excluded equity capital (as defined in section 438 (e) and in paragraphs (c) and (d) of this section) paid in before the beginning of the taxable year and after the beginning of the taxpayer's first taxable year ending after June 30, 1950, exceeds (2) the equity capital at the beginning of such first taxable year ending after June 30, 1950. The amount of the equity capital at the beginning of any taxable year shall be determined as of the beginning of the first day of such taxable year, and shall be determined under section 437 (c) and under the rules applicable to section 437 (c). See section 441 and section 470.

(f) The daily new capital addition for any day includes 75 percent of the amount, if any, by which the increase in the daily borrowed capital for such day exceeds the increase in the excluded borrowed capital for such day. This amount for any day shall be determined by computing:

(1) The amount, if any, by which the daily borrowed capital for such day (as defined in section 439 (b)) exceeds the daily borrowed capital for the first day of the taxpayer's first taxable year ending after June 30, 1950.

(2) The amount by which the excluded borrowed capital for such day exceeds the excluded borrowed capital for the first day of the taxpayer's first taxable year ending after June 30, 1950.

(3) The amount by which subparagraph (1) of this paragraph exceeds subparagraph (2) of this paragraph. Seventy-five percent of the amount so computed is included in the daily new capital addition.

For the purpose of the above computation, the term "excluded borrowed capital" for any day of any taxable year means so much of the daily borrowed capital for such day as consists of outstanding indebtedness to a member of a controlled group, as defined in section 438 (e) (2), which includes the taxpayer.

§ 40.438–3 *Determination of daily new capital reduction.* (a) The daily new capital reduction for any day of the taxable year is the sum of the amounts described in the paragraphs (b) to (d) of this section.

(b) The daily new capital reduction for any day includes distributions to shareholders previously made during such taxable year which are not out of the earnings and profits of such taxable year. For each day of the taxable year, the daily amount of distributions not out of earnings and profits of such year is the total amount of such distributions made during the year and prior to such day. See section 441 for rules applicable in determining the amount of such distributions.

(c) The daily new capital reduction for any day includes the amount, if any, by which (1) the sum of (i) the amount of the equity capital at the beginning of the taxpayer's first taxable year ending after June 30, 1950, and (ii) the total amount of excluded equity capital paid in after the beginning of such first taxable year and before the beginning of the taxable year exceeds (2) the amount of the equity capital at the beginning of the taxable year. Equity capital and excluded equity capital shall be determined in the manner provided in § 40.438–2.

(d) The daily new capital reduction for any day includes 75 percent of the amount, if any, by which the daily borrowed capital (as defined in section 439 (b)) for the first day of the taxpayer's first taxable year ending after June 30, 1950, exceeds the daily borrowed capital (as defined in section 439 (b)) for such day of the taxable year.

§ 40.438–4 *Computation of net new capital addition*—(a) *In general.* The net new capital addition to which the 12 percent credit provided in section 438 (a) shall be applied is the excess, divided by the number of days in the taxable year, of the aggregate of the daily new capital additions for each day of the taxable year over the aggregate of the daily new capital reductions for each day of the taxable year, reduced, however, by the amount determined under paragraphs (1) and (2) of section 438 (b) and under paragraph (b) of this section, relating to an increase in inadmissible assets for the taxable year.

(b) *Limitations under paragraphs (1) and (2) of section 438 (b).* (1) The amount of the reduction applicable in computing the net new capital addition for the taxable year is computed as follows:

(i) The average inadmissible assets for the taxable year is determined by ascertaining the total of the daily amounts attributable to the inadmissible assets for such taxable year, determined under subparagraph (2) of this paragraph, and by dividing such total by the number of days in such taxable year.

(ii) The total of the inadmissible assets for the first day of the taxpayer's first taxable year ending after June 30, 1950, is determined.

(iii) The excess of the average determined in subdivision (i) over the total determined in subdivision (ii) of this subparagraph is ascertained.

(iv) The net new capital addition is computed without including in the daily new capital addition for any day any amount determined under section 438 (c) (3), relating to increases in borrowed capital, and without including in the daily new capital reduction for any day any amount determined under section 438 (d) (3) relating to decreases in borrowed capital.

(v) If the amount ascertained under subdivision (iii) exceeds the amount computed under subdivision (iv) of this subparagraph, then 25 percent of such excess is computed.

(vi) The amount ascertained under subdivision (iii), minus the amount, if any, computed under subdivision (v) of this subparagraph, is the amount of the reduction applicable in computing the net new capital addition.

(2) The amount attributable to inadmissible assets for any day shall be determined under section 440 (b). The ratio of such assets to total assets provided in section 440 (b) is not applicable for the purpose of section 438.

SEC. 439. BORROWED CAPITAL.

(a) *Average borrowed capital.* For the purposes of this subchapter, the average borrowed capital for any taxable year shall be the aggregate of the daily borrowed capital for each day of such taxable year, divided by the number of days in such taxable year.

(b) *Daily borrowed capital.* For the purposes of this subchapter, the daily borrowed capital for any day of any taxable year shall be determined as of the beginning of such day and shall be the sum of the following:

(1) The amount of the outstanding indebtedness (not including interest) of the taxpayer, incurred in good faith for the purposes of the business, which is evidenced by a bond, note, bill of exchange, debenture, certificate of indebtedness, mortgage, deed of trust, bank loan agreement, or conditional sales contract. In the case of property of the taxpayer subject to a mortgage or other lien, the amount of indebtedness secured by such mortgage or lien shall be considered as an indebtedness of the taxpayer whether or not the taxpayer assumed or agreed to pay such indebtedness, plus

(2) In the case of an insurance company, an amount equal to 66⅔ per centum of the mean of the amount of the pro rata unearned premiums determined at the beginning and end of the taxable year, plus,

(3) In the case of a life insurance company, an amount equal to 66⅔ per centum of the mean of the amount of the adjusted reserves, and an amount equal to 66⅔ per centum of the mean of the amount of the reserves on insurance or annuity contracts (or contracts arising out of insurance or annuity contracts) which do not involve, at the time with reference to which the computation was made, life, health, or accident contingencies, determined at the beginning and end of the taxable year; plus

(4) In the case of a face-amount certificate company as defined in section 4 (1) of the Investment Company Act of 1940 (15 U. S. C., section 80a–4), an amount equal to 66⅔ per centum of the mean of the amount of reserves on its outstanding investment certificates, determined at the beginning and end of the taxable year.

§ 40.439–1 *Borrowed capital.* (a) The amount of the average borrowed capital of a corporation shall be computed in the manner provided in section 439 (a) and the daily borrowed capital, as defined in sections 439 (b) (1), (2), (3), and (4), shall be computed in the manner provided in section 439 (b). The average borrowed capital for any taxable year is the aggregate of the daily borrowed capital for each day of the taxable year, divided by the number of days in such taxable year. Daily borrowed capital for any day of the taxable year shall be determined as of the beginning of such day and shall be the sum of the following amounts:

(1) The amount of the outstanding indebtedness (other than interest) of the taxpayer, incurred in good faith for the purpose of the business, which is evidenced by a bond, promissory note, bill of exchange, debenture, certificate of indebtedness, mortgage, deed of trust, bank loan agreement, or conditional sales contract, plus

(2) In the case of an insurance company (except a mutual insurance company other than life or marine) an amount equal to 66⅔ percent of the mean of the amount of its pro rata unearned premiums (see section 204 (b) (5) and § 29.204–2 of Regulations 111) determined at the beginning and end of the taxable year, plus

(3) In the case of a life insurance company, an amount equal to 66⅔ percent of the mean of the amount of the adjusted reserves (see section 201 (c) (3) and § 29.201–6 of Regulations 111), and an amount equal to 66⅔ percent of the mean of the amount of the reserves on insurance or annuity contracts (or contracts arising out of insurance or annuity contracts) which do not involve, at the time with reference to which the computation was made, life, health, or accident contingencies, determined at the beginning and end of the taxable year, plus

(4) In the case of a face-amount certificate company as defined in section 4 (1) of the Investment Company Act of 1940 (15 U. S. C., section 80a–4), an amount equal to 66⅔ percent of the mean of the amount of reserves on its outstanding investment certificates, determined at the beginning and end of the taxable year.

(b) The provisions of section 439 (b) (2) and (3) do not apply to mutual insurance companies other than life or marine. For computation of invested capital in the case of such corporations, see section 437 (b) (3) and § 40.437–4.

(c) Where property of the taxpayer is subject to a mortgage or other lien, the indebtedness secured by the mortgage or lien is considered as the indebtedness of the taxpayer whether or not the taxpayer assumed the mortgage or agreed to pay the indebtedness. If indebtedness of the taxpayer is assumed by another person it ceases to be borrowed capital of the taxpayer. For such purpose an assumption of indebtedness includes the receipt of property subject to indebtedness.

(d) In order for any indebtedness to be included in borrowed capital it must be incurred in good faith for the purposes of the business and not merely to increase the excess profits credit.

(e) Whether outstanding certificates designated by such names as "debenture preferred stock" or "guaranteed preferred stock" constitute borrowed capital depends upon whether the holder has a proprietary interest in the corporation or has the rights of a creditor, determined in the light of all the facts. The name borne by the certificate is of little importance. More important attributes to be considered are whether or not there is a maturity date, the source of payment of any "interest" or "dividend" specified in the certificate (whether only out of earnings or out of capital and earnings), rights to enforce payment, and other rights as compared with those of general creditors.

(f) The term "certificate of indebtedness" includes only instruments having the general character of investment securities issued by a corporation as distinguishable from instruments evidencing debts arising in ordinary transactions between individuals. The term "conditional sales contract" means a contract corresponding to a mortgage except that the transfer of title is made dependent upon the payment of the stipulated price. Borrowed capital does not include indebtedness incurred by a bank arising out of the receipt of a deposit and evidenced, for example, by a certificate of deposit, a passbook, a cashier's check, or a certified check, and the term "bank loan agreement" does not include the indebtedness of a bank to a depositor.

SEC. 440. ADMISSIBLE AND INADMISSIBLE ASSETS.

(a) *Definitions.* For the purposes of this subchapter—

(1) The term "inadmissible assets" means—

(A) Stock in corporations, except stock in a foreign personal holding company, and except stock which is not a capital asset; and

(B) Obligations described in section 22 (b) (4) any part of the interest from which is excludible from gross income or allowable as a credit against net income.

(2) The term "admissible assets" means all assets other than inadmissible assets.

(b) *Ratio of inadmissibles to total assets.* In the case of any amount which is required to be reduced by reference to this subsection, the reduction shall be the same percentage of such amount as the percentage which the total of the inadmissible assets is of the total of admissible and inadmissible assets. For such purposes, the amount attributable to each asset held at any time during such taxable year shall be determined by ascertaining the adjusted basis thereof (or, in the case of money, the amount thereof) for each day of such taxable year so held and adding such daily amounts. The determination of such daily amounts shall be made as of the beginning of each day under regulations prescribed by the Secretary. The adjusted basis shall be the adjusted basis for determining gain upon sale or exchange as determined under section 113.

§ 40.440–1 *Admissible and inadmissible assets.* (a) Adjustments for "inadmissible assets" are required under section 435 (f) and section 435 (g), relating to the computation of the excess profits credit under the income method. Adjustments for such assets must be made under sections 436 (a) (1) and 438 (b), relating to the computation of the excess profits credit under the invested capital method. Adjustment for such assets must also be made under section 448 (b) (3), relating to the computation of the excess profits credit in the case of certain regulated public utilities. See also section 442 (f).

(b) The term "inadmissible assets" means (1) stock in all corporations,

domestic or foreign, except stock in a foreign personal holding company, and except stock which is not a capital asset (such as stock held primarily for sale to customers by a dealer in securities), and (2) all obligations described in section 22 (b) (4), any part of the interest from which is excludible from gross income or allowable as a credit against net income. Stock held in the treasury of the issuing corporation is an inadmissible asset. The term "admissible assets" means all assets other than inadmissible assets.

(c) Section 440 (b) contains provisions for determining the amount of inadmissible assets for any day, and also contains provisions for determining the reductions referred to in section 436 (a) (1) and section 448 (b) (3).

(d) (1) Section 440 (b) provides that the amount attributable to inadmissible assets for any day shall be determined under regulations and shall be determined as of the beginning of such day. The amount attributable for any day to any inadmissible asset is the adjusted basis thereof in the hands of the taxpayer at the beginning of such day. See section 441 and section 470 for rules applicable in determining such adjusted basis. The total inadmissible assets for any day, and the daily amount attributable to all inadmissible assets for any day, is the aggregate of the amounts attributable to inadmissible assets for such day.

(2) If the aggregate of the total inadmissible assets for each day of the taxable year must be computed (see, for example, section 435 (g) (5) (A)), and if it is impracticable to determine such amounts as of the beginning of each day but the amounts held on a given day of each month throughout the year or at other regular intervals not exceeding one year can be determined, the amounts held as of the beginning of each day of such month or other period may be determined by dividing by two the sum of the amounts of such assets held at the beginning of the period and the amounts held at the end of the period. If at any time a substantial change has taken place in the amount of inadmissible assets, the effect of such change shall be averaged exactly from the date on which it occurred. Ordinarily the taxpayer will be able to determine the amount of inadmissible assets actually held on each day of the taxable year. The fact that it may be impracticable to determine the amount of admissible assets actually held on each day of the taxable year will not relieve the taxpayer from the necessity of determining the actual amount of inadmissible assets held unless such determination is likewise impracticable.

(e) The amount attributable to admissible assets for any day shall be determined in the same manner as that provided in paragraph (c) of this section with respect to inadmissible assets. In the case of money the amount thereof is included in the computation under section 440.

(f) Section 440 (b) also provides the method for determining the amount of the reductions referred to in section 436 (a) (1) and section 448 (b) (3). For the purpose of such reductions, the aggregate of the daily amounts attributable to inadmissible assets and the aggregate of the daily amounts attributable to admissible assets are computed. The amount which bears the same ratios to the amount which is required to be reduced by reference to section 440 (b) as such aggregate of the inadmissible assets bears to such aggregate of the inadmissible and admissible assets is then determined. The amount so determined is the amount of the reduction referred to in section 436 (a) (1) or section 438 (b) (3), as the case may be.

SEC. 441. RULES FOR DETERMINING CREDIT. For the purposes of this section, section 435, section 437, section 438, and section 440—

(a) *Equity capital.* The term "equity capital" means the equity capital as defined in section 437 (c).

(b) *Property paid-in.* For the purpose of determining the amount of property paid in for stock, or as a paid-in surplus, or as a contribution to capital, such property shall be included in an amount equal to its basis (unadjusted) for determining gain upon sale or exchange. If the unadjusted basis of the property is a substituted basis, such basis shall be adjusted, with respect to the period before the property was paid in, by an amount equal to the adjustments proper under section 113 (b) (2).

(c) *Money and property paid-in.* For the purpose of determining the amount of money and property paid in for stock, or as paid-in surplus, or as a contribution to capital, there shall be included only money and property paid in good faith for the purposes of the taxpayer's business.

(d) *Distributions to shareholders.* A distribution by a corporation of its stock or rights to acquire its stock shall not be regarded as money or property paid in for stock, or as paid-in surplus, or as a contribution to capital, and such a distribution shall not be considered as a distribution by a corporation to its shareholders.

(e) *Distributions in first 60 days of taxable year.* So much of the distributions (taken in the order of time) to shareholders made during the first 60 days of any taxable year as does not exceed the accumulated earnings and profits as of the beginning thereof (computed without regard to this paragraph) shall be considered to have been made on the last day of the preceding taxable year. This paragraph shall not apply with respect to distributions made during the first 60 days of the taxpayer's first taxable year under this subchapter.

(f) *Computation of earnings and profits of taxable year.* In determining whether a distribution is out of the earnings and profits of any taxable year, such earnings and profits shall be computed as of the close of such taxable year without diminution by reason of any distribution made during such taxable year or by reason of the tax under this chapter for such year and the determination shall be made without regard to the amount of earnings and profits at the time the distribution was made.

(g) *Exchanges.* For the purpose of determining the amount of property paid in for stock, or as paid-in surplus, or as a contribution to capital—

(1) If the basis (unadjusted) of the property for determining gain upon a sale or exchange is determined by reference to the basis of the property in the hands of the transferor, proper adjustment shall be made for the amount of any liability of the transferor assumed upon the exchange and of any liability subject to which such property was so received, for the amount of any other liability of the taxpayer constituting consideration for the property so received, and for the aggregate of the amount of money and the fair market value of other property (other than such stock and other than such liabilities) transferred to the transferor.

(2) If an indebtedness of the taxpayer is canceled or released in exchange for stock, or as paid-in surplus, or as a contribution to capital, the amount paid in shall be considered equal to the amount of the indebtedness.

(h) *Election under section 455.* In the case of a taxpayer electing under section 455, the invested capital, the net new capital addition, the base period capital addition determined under section 435 (f), and the net capital addition or reduction determined under section 435 (g) shall be computed in a manner consistent with the method of accounting so elected, except as to installment sales made (or installment sales obligations acquired) prior to the first taxable year under this subchapter in the case of a taxpayer electing under section 455 (a), and except as to contracts begun before the first taxable year under this subchapter in the case of a taxpayer electing under section 455 (b).

(i) *Effect of intangible property on determination of credit.* In the case of intangible property, the basis (unadjusted) and the adjusted basis for determining gain upon sale or exchange shall be determined without regard to the value of the property as of March 1, 1913. For the purposes of this subsection, the term "intangible property" means secret processes and formulae, good will, trade-marks, trade brands, franchises, and other like property. The provisions of this subsection shall not apply in determining the amount of gain realized upon the sale, exchange, or other disposition of such property.

(j) *Improvements by lessee to properties of lessor railroad corporation.*—For the purposes of section 437 (c), the fair value of additions and betterments made by the lessee to the physical properties of a lessor railroad corporation which have become the property of the lessor corporation by rejection of its lease (such fair value being determined as of the date such additions and betterments became the property of the lessor) shall be included in determining the basis (unadjusted) of such property; and where the value of such improvements cannot be accurately determined by the old records thereof, because lost, incomplete, or inaccurate, the value of such improvements determined by the Interstate Commerce Commission for rate-making purposes shall be used in lieu of such fair value.

§ 40.441-1 *Rules for determining credit*—(a) *In general.* Section 441 provides rules applicable for the purposes of sections 435, 437, 438, and 440 in determining the excess profits credit for any taxable year by reference to any of such sections. Furthermore, each rule set forth in section 441 is subject to the other rules provided by that section.

(b) *Equity capital.* The term "equity capital" means the equity capital as defined in section 437 (c).

(c) *Money and property paid in.* For the purpose of determining the amount of money and property paid in for stock, or as paid-in surplus, or as a contribution to capital, there shall be included only money and property paid-in in good faith for the purposes of the taxpayer's business. Where property is paid in for stock, or as paid-in surplus or as a contribution to capital, the amount of any property shall be the unadjusted basis to the taxpayer for determining gain upon a sale or exchange. If the unadjusted basis of the property is a substituted basis, such basis shall be adjusted with respect to the period before the

property was paid in, by an amount equal to the adjustments proper under section 113 (b) (2).

(d) *Distributions to shareholders.* Subject to the rule provided in section 441 (e) and in paragraph (e) of this section, a distribution is considered to be made on the date it is payable, except that where no date is set for its payment, the distribution is considered to be made on the date when it is declared. A distribution by a corporation in its stock, or in rights to acquire its stock shall not be regarded as money or property paid in for stock, or as paid-in surplus, or as a contribution to capital, whether such a distribution is paid out of capital or out of earnings and profits, or is of such a character as to be subject to tax in the hands of a distributee because not exempt as a stock dividend either by statute or otherwise. Such a distribution is not deemed to constitute a distribution by a corporation to its shareholders and does not reduce the adjusted invested capital or the equity capital of the taxpayer at any time.

(e) *Distributions in first 60 days of taxable year.* In computing invested capital, equity capital, or accumulated earnings and profits as of the beginning of any taxable year and in determining what distributions during any taxable year were made out of the earnings and profits of such taxable year, distributions made during the first 60 days of the taxable year (except in the case of the taxpayer's first taxable year ending after June 30, 1950) are deemed, to the extent they do not exceed the accumulated earnings and profits as of the beginning of such taxable year, to have been made on the last day of the preceding taxable year. In applying such rule, such distributions shall be considered in the order of time. For example, if a corporation on the calendar year basis has accumulated earnings and profits of $100,000 on January 1, 1951, and makes distributions of $75,000 on January 15, 1951, and $60,000 on February 15, 1951, the distribution of January 15, 1951, and $25,000 of the distribution of February 15, 1951, are considered as having been made on December 31, 1950.

(f) *Computation of earnings and profits of taxable year.* In determining whether a distribution is out of the earnings and profits of any taxable year, such earnings and profits shall be computed as of the close of such taxable year without diminution by reason of any distribution made during such taxable year, or by reason of any income or excess profits tax imposed for such taxable year, and without regard to the amounts of earnings and profits at the time the distribution was made. For example, if a corporation making a return on the calendar year basis had accumulated earnings and profits as of the beginning of the taxable year of $50,000, and earnings and profits during the taxable year (without diminution by any distributions, or by the income or excess profits tax for the taxable year) of $150,000, all earned during the last six months of the taxable year, and distributed $175,000 as dividends during the taxable year, $56,000 on April 1, $70,000 on July 1, and $49,000 on October 1, six-sevenths of each distribution will be deemed to have been paid out of earnings of the taxable year and one-seventh from accumulated earnings and profits, so that accumulated earnings and profits will be reduced by $8,000 beginning April 2, by an additional $10,000 beginning July 2, and by an additional $7,000 beginning October 2.

(g) *Exchanges.* (1) For the purpose of determining the amount of property paid in for stock, or as paid-in surplus, or as a contribution to capital, if the unadjusted basis of the property for determining gain upon a sale or exchange is determined by reference to the basis of the property in the hands of the transferor, such amount shall be reduced by the sum of the following:

(i) The amount of any liability of the transferor assumed upon the exchange and of any liability subject to which such property was so received,

(ii) The amount of any liability of the transferee (not arising out of any liability described in subdivision (i) of this subparagraph) constituting consideration for the property so received, and

(iii) The aggregate of the amount of any money and the fair market value of any other property (other than such stock and other than property described in subdivisions (i) and (ii) of this subparagraph) transferred to the transferor, whether or not such money or property was permitted to be received by the transferor without the recognition of gain.

(2) Where indebtedness of a taxpayer is cancelled or released in exchange for stock, or as paid-in surplus, or as a contribution to capital, the amount paid in shall be considered equal to the amount of the indebtedness. For example, if a corporation exchanges stock for bonds outstanding in a transaction in which, if property other than bonds were paid in, such property would have the same basis in the hands of the taxpayer as in the hands of the transferor, the face amount of the bonds, rather than their basis in the hands of the bondholder, is treated as the amount paid in for such stock.

(h) *Election under section 455.* In the case of a taxpayer electing under section 455 (a) to compute its income from installment sales or installment sales obligations on the basis of the taxable period for which such income is accrued, and in the case of a taxpayer electing under section 455 (b) to compute income from long-term contracts on the percentage of completion method of accounting, section 441 (h) provides that the invested capital, the net new capital addition, the base period capital addition, and the net capital addition or reduction shall be computed in a manner consistent with the method of accounting so elected. However, for the purpose of such computations, installment sales made, or installment sales obligations acquired, prior to the beginning of the taxpayer's first taxable year ending after June 30, 1950, shall be taken into account as if the taxpayer continued to report income on the installment basis, and long-term contracts begun prior to the beginning of the taxpayer's first taxable year ending after June 30, 1950, shall be taken into account as if the taxpayer continued to report income on the completed contract basis. For example, if a taxpayer on the calendar year basis elects under section 455 (a) to use the accrual method of accounting for excess profits tax purposes, its equity capital as of the beginning of its 1950 taxable year is computed by treating its accounts receivable with respect to installment sales as having an adjusted basis determined under section 44 (d), and its equity capital as of the beginning of its taxable year 1951 would be computed by determining the adjusted basis of its accounts receivable with respect to installment sales made before 1950 in the same manner as the computation for 1950, and by determining the adjusted basis of its accounts receivable with respect to installment sales made after 1949 (which are reported on the accrual basis for excess profits tax purposes) in the same manner as in the case of a taxpayer reporting on the accrual basis for all purposes. Another example might be a taxpayer on the calendar year basis electing under section 455 (b) to compute income from long-term contracts by using the percentage of completion method of accounting. For the purpose of determining the base period capital addition of such taxpayer, the election would have no effect (since all contracts involved would have been begun prior to January 1, 1950) and the completed contract method of accounting would apply to all items entering into the computation. However, for purposes of determining the net capital addition or reduction of the taxpayer for 1950, contracts begun in 1950 would be accounted for on the percentage of completion method of accounting whereas contracts begun prior to 1950 and completed in 1950 or in a subsequent year would be accounted for on the completed contract method of accounting. The amount of normal tax and surtax for any taxable year is not recomputed under section 441 (h) for any purpose. If average base period net income is computed under section 442, 443, 444, 445, or 446, the computation of total assets for the purpose of such section shall be made subject to the rules provided in section 441 (h). The determination of the recent loss adjustment under section 437 (f) is made on the basis of the taxpayer's former method of accounting unless the recent loss period ends on a date later than the beginning of the taxpayer's first taxable year ending after June 30, 1950, in which case the net income or net operating loss for such taxable year shall be computed on the basis of the method of accounting elected under section 455, subject to the rules provided in section 441 (h) and in this section.

(i) *Effect of intangible property on determination of credit.* In the case of intangible property, both the unadjusted and adjusted basis for determining gain upon sale or exchange shall be determined without regard to the value of the property as of March 1, 1913. However, this rule shall not have any application in determining the amount of gain realized upon the sale (exchange, or other disposition of such property. As used in section 441 (i), the term "intangible property" means secret processes and formulas, good will, trade-

marks, trade brands, franchises, and other like property.

(j) *Improvements by lessee to properties of lessor railroad corporation.* For the purpose of computing equity capital under section 437 (c), the fair value of additions and betterments made by the lessee to the physical properties of the lessor, having become the property of the lessor by rejection of its lease, is included in determining the unadjusted basis of such property. The specific rules for determination of such fair value are set forth in section 441 (j).

SEC. 442. AVERAGE BASE NET INCOME—ABNORMALITIES DURING BASE PERIOD.

(a) *In general.* If a taxpayer which commenced business on or before the first day of its base period establishes that, for any taxable year within, or beginning or ending within, its base period:

(1) Normal production, output, or operation was interrupted or diminished because of the occurrence, either immediately prior to, or during such taxable year, of events unusual and peculiar in the experience of such taxpayer, or

(2) The business of the taxpayer was depressed because of temporary economic circumstances unusual in the case of such taxpayer,

the taxpayer's average base period net income determined under this section shall be the amount computed under subsection (c) or (d), whichever is applicable.

(b) *Period subject to adjustment.* The period subject to adjustment under this section shall be determined as follows:

(1) By computing the excess profits net income or deficit in excess profits net income for each month in the base period. The excess profits net income or the deficit in excess profits net income for any month shall be the excess profits net income or deficit in excess profits net income, as the case may be, for the taxable year in which such month falls divided by the number of calendar months in such year.

(2) By eliminating from the base period whichever of the following 12 months results in the higher remaining aggregate excess profits net income or the lower remaining aggregate deficit in excess profits net income—

(A) The 12 consecutive months the elimination of which produces the highest remaining aggregate excess profits net income, or the lowest remaining aggregate deficit in excess profits net income, or

(B) The 12 months which remain after retaining in the base period the 36 consecutive months which produce the highest remaining aggregate excess profits net income or the lowest remaining aggregate deficit in excess profits net income.

(c) *Twelve or fewer months affected by abnormalities.* If no more than 12 of the months remaining after the application of subsection (b) (2) fall within taxable years the excess profits net income of which was reduced (or the deficit in excess profits net income of which was increased) by reason of an abnormality determined to exist under subsection (a), the average base period net income determined under this section shall be computed as follows:

(1) By computing the excess profits net income, determined in accordance with section 435 (d) (1), for each of the 36 months remaining after the application of subsection (b) (2) of this section.

(2) By computing, for each such month which falls within any taxable year the excess profits net income of which was reduced (or the deficit in excess profits net income of which was increased) by reason of an abnormality determined to exist under subsection (a), the substitute excess profits net income provided under subsection (e).

(3) By identifying the months described in paragraph (2) for which the amount of the substitute excess profits net income ascertained under such paragraph exceeds 110 per centum of the amount of the excess profits net income ascertained under paragraph (1).

(4) By computing the sum of (A) the aggregate of the substitute excess profits net income for each of the months identified under paragraph (3) and (B) the aggregate of the excess profits net income (ascertained under paragraph (1)) for each of the other months remaining after the application of subsection (b) (2).

(5) By dividing by 3 the amount ascertained under paragraph (4).

(d) *More than twelve months affected by abnormalities.* If more than 12 of the months remaining after the application of subsection (b) (2) fall within taxable years the excess profits net income of which was reduced (or the deficit in excess profits net income of which was increased) by reason of an abnormality determined to exist under subsection (a), the average base period net income determined under this section shall be computed as follows:

(1) By determining the amount of the taxpayer's total assets for the last day of each of its taxable years ending after the first day of its base period and prior to the first day of its first taxable year under this subchapter.

(2) By computing the average of the amounts ascertained under paragraph (1).

(3) By multiplying the amount ascertained under paragraph (2) by the base period rate of return, proclaimed by the Secretary under section 447, for the taxpayer's industry classification.

(4) By determining the aggregate amount of interest paid or incurred by the taxpayer for all taxable years ending after the first day of its base period and prior to the first day of its first taxable year under this subchapter, dividing such aggregate by the total number of months in such years, and multiplying the quotient by 12.

(5) By subtracting the amount ascertained under paragraph (4) from the amount ascertained under paragraph (3).

This subsection shall have no application with respect to any taxpayer unless the amount of the taxpayer's average base period net income determined under this subsection exceeds 110 per centum of the taxpayer's average base period net income computed under section 435 (d).

(e) *Substitute excess profits net income—*(1) *Computation.* For the purposes of subsection (c) (2), the substitute excess profits net income for any month shall be computed as follows:

(A) By multiplying the amount of the taxpayer's total assets for the last day of the taxable year in which such month falls or for the last day of its taxable year immediately preceding its first taxable year under this subchapter, whichever day is earlier, by the rate of return provided under paragraph (2).

(B) By reducing the amount ascertained under subparagraph (A) by the total interest paid or incurred by the taxpayer for the 12 months beginning with the first day of the taxable year within which such month falls.

(C) By dividing by 12 the amount ascertained under subparagraph (B).

(2) *Base period yearly rate of return.* The rate of return to be used under paragraph (1) (A) shall be the base period yearly rate of return, proclaimed by the Secretary under section 447 for the taxpayer's industry classification, for the following year—

(A) In the case of a taxable year of the taxpayer beginning in 1945 and ending in 1946—for the year 1946;

(B) In the case of a taxable year of the taxpayer beginning in 1949 and ending in 1950—for the year 1949; and

(C) In the case of any other taxable year of the taxpayer—for the year in which falls the greater number of days in such taxable year.

(f) *Total assets.* For the purposes of this section, the taxpayer's total assets for any day shall be determined as of the end of such day and shall be an amount equal to the sum of the cash and the property (other than cash, inadmissible assets, and loans to members of a controlled group as defined in section 435 (f) (4) held by the taxpayer in good faith for the purposes of the business. Such property shall be included in an amount equal to its adjusted basis for determining gain upon sale or exchange, determined under the rules provided in section 441.

(g) *Taxpayer's industry classification.* The taxpayer's industry classification shall be determined, for the purposes of subsection (d), by reference to the last taxable year within or beginning within its base period, and, for the purposes of subsection (e), by reference to the taxable year within which falls the last month for which a substitute excess profits net income is determined; and, in either case, shall be the industry classification under section 447 to which is attributable the largest amount of the taxpayer's gross receipts for such taxable year.

(h) *Rules for application of section.* The benefits of this section shall not be allowed unless the taxpayer makes application therefor in accordance with section 447 (e).

(i) *Cross references.* (1) For definition of gross receipts, see section 435 (e) (5).

(2) For computation of capital additions in the base period, see section 435 (f) (3).

(3) For computation of excess profits credit based on income in the case of certain reorganizations, see Part II of this subchapter.

§ 40.442–1 *General rule.* If a taxpayer which commenced business on or before the first day of its base period establishes that it experienced certain abnormalities (described in § 40.442–2), then such taxpayer may be entitled to use the average base period net income computed under section 442. See § 40.442–3, for methods of computation. However, section 442 is applicable only if the taxpayer makes application therefor in accordance with section 447 (e). For rules governing the application of section 442 in the case of an acquiring corporation, see section 462 (d), and in the case of a component corporation, see section 461 (c).

§ 40.442–2 *Abnormalities—*(a) *Interruption or diminution of normal production, output, or operation in the base period.* (1) Section 442 applies if the taxpayer establishes that for any taxable year within, or beginning or ending within, its base period its normal production, output, or operation was interrupted or diminished because of the occurrence either immediately prior to or during such taxable year, of events unusual and peculiar in the experience of the taxpayer. Activities comprised within the meaning of production, output, or operation include the rendering of services in those cases in which corporations render services rather than manufacture or market tangible products, for example, advertising agencies, brokerage concerns, purchasing agents, etc. Normal production, output, or oper-

ation, means the level of production, output, or operation customary for the taxpayer, determined on the basis of the actual experience of the taxpayer up to the time the unusual and peculiar event occurred.

(2) Not every interruption or diminution of normal production, output, or operation in the base period may furnish the basis for the application of section 442 (a) (1). The interruption or diminution must be significant and not trivial.

(3) An event is unusual and peculiar in the experience of the taxpayer if its occurrence is not ordinarily encountered in the taxpayer's business operations. Such event may be unusual in the case of the taxpayer even though it is also unusual in the case of other taxpayers. For example, a flood in a particular locality may be unusual in the case of a number of taxpayers. If an event is unusual in the course of business experience in general but regular in the case of the taxpayer, such event is not unusual and peculiar in the experience of that taxpayer. Thus, if a corporation is engaged in felling and transporting logs and timber, and if its annual operations are interrupted by spring floods occasioned by thaws and rains, such events are not unusual and peculiar in the experience of that corporation. Unusual and peculiar events contemplated in section 442 (a) (1) consist primarily of physical rather than economic events or circumstances. Such physical events include floods, fires, explosions, strikes, and other exceptional and uncommon circumstances hindering production, output, or operation.

(b) *Business depression in base period on account of temporary economic circumstances.* (1) Section 442 applies if the taxpayer establishes that its business was depressed for any taxable year within, or beginning or ending within, its base period because of temporary economic circumstances unusual in the case of such taxpayer. Section 442 (a) (2) applies to only those economic circumstances which were temporary in the sense that they had little perceptible long-range effect upon the taxpayer's business, and which affected the taxpayer unusually as distinguished from those economic events which were of a chronic or continuing character.

(2) As in the case of unusual and peculiar events interrupting or diminishing production, output, or operation, a temporary economic circumstance is unusual in the case of a taxpayer if its occurrence is not ordinarily encountered in that taxpayer's business operations. A temporary economic circumstance may be unusual in the case of a taxpayer even though it is also unusual in the case of other taxpayers. If an economic circumstance is unusual in the course of business experience in general but regular in the case of the taxpayer, such circumstance is not unusual in the case of such taxpayer. An example illustrating section 442 (a) (2) might be a taxpayer compelled to develop a new market because it conducted business with only one customer for a long period of years and lost such customer during the base period when such customer decided to manufacture for itself the product it had formerly bought from the taxpayer.

§ 40.442–3 *Computation of average base period net income*—(a) *Period subject to adjustment.* If a taxpayer which commenced business on or before the first day of its base period qualifies as to abnormalities in its base period under § 40.442–2, the period subject to adjustment is determined under section 442 (b)—

(1) By computing the excess profits net income (or deficit in excess profits net income) for each month in the taxpayer's base period, such computation being made by dividing the excess profits net income (or deficit in excess profits net income) as determined under section 433 (b) (or (c)) for the taxable year in which the month falls, by the number of calendar months in such taxable year, and

(2) Either by eliminating 12 consecutive months, or by eliminating the 12 months remaining after retaining 36 consecutive months, whichever method produces the highest aggregate excess profits net income (or lowest deficit) for the 36 months retained after such elimination of 12 months.

After such determination of the 36 months which result in the highest aggregate excess profits net income (or lowest deficit), the average base period net income is determined by whichever of the methods set forth in paragraphs (b) and (c) of this section is applicable.

(b) *12 or fewer months affected adversely by abnormalities.* If 12 or fewer of the 36 base period months determined under paragraph (a) of this section fall within taxable years which are affected adversely as to excess profits net income by abnormalities determined to exist under section 442 (a) and § 40.442–2, the taxpayer's average base period net income is computed under section 442 (c) as follows:

(1) An excess profits net income is computed under section 435 (d) (1) for each of the 36 base period months, by dividing the excess profits net income for the taxable year in which each such month falls by the number of full calendar months in such taxable year, and raising any deficits in excess profits net income to zero.

(2) The substitute excess profits net income is computed for each such month which falls within a taxable year affected adversely as to excess profits net income by such abnormalities. The substitute excess profits net income is computed under section 442 (e) for each such month as follows:

(i) The taxpayer's total assets (determined under section 442 (f) and under paragraph (d) of this section) for the last day of the taxable year in which such month falls, or for the last day of the taxpayer's last taxable year ending before July 1, 1950, whichever day is earlier, is multiplied by the appropriate industry base period yearly rate of return determined under section 447 for the base period year in which such month falls. See section 442 (e) (2) for special rules in case of fiscal years. Under section 442 (g) the appropriate industry classification under section 447 is the classification to which is attributable the largest amount of the taxpayer's gross receipts for the taxable year within which falls the last month for which a substitute excess profits net income is determined.

(ii) The amount determined under subdivision (i) of this subparagraph is reduced by the total interest paid or incurred by the taxpayer for the 12 months beginning with the first day of the taxable year within which such month falls.

(iii) The amount determined under subdivision (i) and reduced under subdivision (ii) of this subparagraph is divided by 12. The amount so computed is the substitute excess profits net income for the month.

(3) Each month for which the substitute excess profits net income determined under subparagraph (2) exceeds 110 percent of the excess profits net income determined under subparagraph (1) of this paragraph is identified.

(4) The aggregate of the substitute excess profits net income for the months identified in subparagraph (3) is added to the aggregate of the excess profits net income, ascertained under subparagraph (1), for those of the 36 base period months which were not identified under subparagraph (3) of this paragraph.

(5) The sum ascertained under subparagraph (4) of this paragraph is divided by 3. The result obtained is the average base period net income determined under section 442.

(c) *More than 12 months affected adversely by abnormalities.* If more than 12 of the 36 base period months fall within taxable years which are affected adversely as to excess profits net income by abnormalities determined to exist under section 442 (a) and § 40.442–2, the taxpayer's average base period net income is computed under section 442 (d) as follows:

(1) The amount of the total assets for the last day of each taxable year ending after the first day of the taxpayer's base period and prior to July 1, 1950, is determined under section 442 (f) and under paragraph (d) of this section.

(2) The sum of the amounts ascertained under subparagraph (1) of this paragraph is divided by the number of such amounts.

(3) The average ascertained under subparagraph (2) of this paragraph is multiplied by the base period rate of return determined under section 447 for the taxpayer's industry classification. Under section 442 (g) the taxpayer's industry classification is the classification to which is attributable the largest amount of the taxpayer's gross receipts for its last taxable year beginning within its base period.

(4) The average of the aggregate interest paid or incurred by the taxpayer for all taxable years ending after the first day of its base period and prior to July 1, 1950, is subtracted from the amount determined under subparagraph (3) of this paragraph. This average is computed by ascertaining the total of such interest for all such taxable years, by dividing the amount so ascertained by the number of months in such taxable years, and by multiplying the quotient by 12.

The amount determined under subparagraphs (1)–(4) of this paragraph, is the average base period net income computed under section 442 only if such amount exceeds 110 percent of the taxpayer's average base period net income computed under section 435 (d). If such amount does not exceed 110 percent of such average, section 442 is not applicable to the taxpayer.

(d) *Definitions.* For the purpose of section 442—

(1) The term "total assets" for any day means the sum of the cash and other property (other than inadmissible assets, as defined in section 440 (a) (1), and other than loans to members of a controlled group, as defined in section 435 (f) (4)) held by the taxpayer at the end of such day in good faith for purposes of the business. Property shall be included in an amount equal to its adjusted basis for determining gain upon sale or exchange, except that the adjusted basis of secret processes and formulas, good will, trade-marks, trade brands, franchises, and other like property shall be determined without regard to value as of March 1, 1913. In determining total assets, so much of the distributions to shareholders made during the first 60 days of any taxable year (other than the taxpayer's first taxable year ending after June 30, 1950) as does not exceed the accumulated earnings and profits at the beginning of the year shall be considered to have been made on the last day of the preceding taxable year. For special rule in the case of improvements by a lessee to properties of a lessor railroad corporation, see section 441 (j). In the case of a taxpayer electing to compute income from installment sales or installment sales obligations on the accrual method of accounting, or income from long-term contracts on the percentage of completion method of accounting, see section 441 (h). See section 470 for rules applicable in determining the adjusted basis of assets received in certain intercorporate liquidations.

(2) The term "gross receipts" means gross receipts as defined in section 435 (e) (5).

(3) For rules for determining when a taxpayer "commenced business," see § 40.445–1.

(4) The term "base period" means the base period as defined in section 435 (b).

(5) The term "interest" includes interest on all indebtedness, irrespective of whether the indebtedness constitutes borrowed capital within the meaning of section 439 (b).

(e) *Cross reference.* For special rules in determining the base period capital addition in case average base period net income is computed under section 442, see section 435 (f) (3) and § 40.435–6 (d).

SEC. 443. AVERAGE BASE PERIOD NET INCOME—CHANGE IN PRODUCTS OR SERVICES.

(a) *In general.* If a taxpayer which commenced business on or before the first day of its base period establishes with respect to any taxable year that—

(1) During so much of its three immediately preceding taxable years as falls within the 36-month period ending on the last day of its base period, there was a substantial change in the products or services furnished by the taxpayer.

(2) More than 40 per centum of its gross income or 33 per centum of its net income for such taxable year is attributable to one or more of the new products or services, and

(3) Its average monthly excess profits net income (determined under subsection (e)) for such taxable year exceeds 125 per centum of its average monthly excess profits net income (determined under subsection (e)) for the taxable years ending within its base period and prior to the taxable year in which the first change to which gross income is attributed for the purpose of this subsection occurred,

then, in computing its excess profits credit for taxable years under this subchapter which end on or after the last day of the earliest taxable year with respect to which the requirements of paragraphs (1), (2), and (3) are satisfied, its average base period net income determined under this section shall be the amount computed under subsection (b).

(b) *Average base period net income.* The average base period net income determined under this section shall be computed as follows:

(1) By multiplying the amount of the taxpayer's total assets for (A) the last day of its taxable year immediately preceding its first taxable year under this subchapter, or (B) the last day of the taxable year in which the taxpayer first meets the requirements of subsection (a), whichever day is later, by the base period rate of return, proclaimed by the Secretary under section 447, for the taxpayer's industry classification.

(2) By subtracting from the amount ascertained under paragraph (1) the total interest paid or incurred by the taxpayer for the 12 months ending with whichever day is used under such paragraph.

(c) *Taxpayer's industry classification.* For the purposes of this section, the taxpayer's industry classification shall be the industry classification under section 447 to which is attributable the largest amount of the taxpayer's gross receipts for the taxable year which includes whichever day is used under subsection (b).

(d) *Capital addition or reduction.* If the average base period net income of the taxpayer is determined under this section—

(1) The excess profits credit for the taxable year in which the taxpayer first meets the requirements of subsection (a) shall not include any net capital addition or reduction determined under section 435 (g), and

(2) In determining the net capital addition or reduction under section 435 (g) for any subsequent taxable year, the expression "the first day of the taxpayer's first taxable year under this subchapter" shall be read as "the first day of the taxpayer's first taxable year under this subchapter or the day following the close of the taxable year in which the taxpayer first met the requirements of section 443 (a), whichever day is later".

(e) *Average monthly excess profits net income.* For the purposes of subsection (a) (3)—

(1) The excess profits net income for any year shall be computed by making the adjustments provided in section 433 (b) as though such section were applicable to all taxable years.

(2) The average monthly excess profits net income for any period of two or more taxable years shall be determined (A) by computing the aggregate of the excess profits net income for all taxable years within such period, (B) by subtracting from such aggregate the aggregate amount of the deficits in excess profits net income for all taxable years within such period, and (C) by dividing the amount ascertained under (B) by the total number of months in such taxable years.

(3) The average monthly excess profits net income determined for any period shall in no case be less than zero.

(f) *Rules for application of section.* The benefits of this section shall not be allowed unless the taxpayer makes application therefor in accordance with section 447 (e).

(g) *Cross references.* (1) For definition of gross receipts, see section 435 (e) (5).

(2) For definition of total assets, see section 442 (f).

(3) For computation of excess profits credit based on income in the case of certain reorganizations, see Part II of this subchapter.

§ 40.443–1 *General rule.* (a) A taxpayer which commenced business on or before the first day of its base period and which, during the last 36 months of its base period, changed substantially the products or services furnished by it may, in certain cases, compute its average base period net income under section 443. The taxpayer must establish, with respect to a single taxable year (hereinafter referred to as the "qualifying taxable year"), that—

(1) During so much of its three immediately preceding taxable years as falls within the 36-month period ending on the last day of its base period, there was a substantial change in the products or services furnished by the taxpayer, and

(2) Either more than 40 percent of its gross income or more than 33 percent of its net income for the qualifying taxable year is attributable to one or more of the new products or services, and

(3) Its average monthly excess profits net income for the qualifying taxable year exceeds 125 percent of its average monthly excess profits net income for the taxable year (or years) ending within its base period and ending prior to the taxable year in which occurred the first change in products or services to which gross income or net income is attributed for the purpose of the requirement of subparagraph (2) of this paragraph.

(b) The qualifying taxable year may be a base period taxable year or a taxable year ending after June 30, 1950, but in any case shall be the earliest taxable year with respect to which the taxpayer meets the requirements of subparagraphs (1), (2), and (3) of this paragraph. A taxpayer meeting the requirements of subparagraphs (1), (2), and (3) of this paragraph may compute its average base period net income under section 443 for the qualifying taxable year (if an excess profits tax taxable year) and for each subsequent excess profits tax taxable year. Under section 443, the average base period net income is computed on the basis of the base period rate of return for the taxpayer's industry classification. See § 40.443–3 (a) for method of computation. However, section 443 is applicable only if the taxpayer makes application therefor in accordance with section 447 (e). For rules governing the application of section 443 in the case of an acquiring corporation, see section 462 (e), and in the case of a component corporation, see section 461 (c).

§ 40.443–2 *Requirements as to change in products or services*—(a) *Substantial change in products or services.* (1) For the purpose of section 443, there is a change in products or services only if the new products or services are substan-

tially different from the products or services previously furnished. Ordinarily, it is necessary that the trade custom or practice treat the new products or services as being of a different class from the products or services previously furnished by the taxpayer. A mere improvement or change in style of product or service does not constitute a change in the product or service. The change must represent more than a usual or customary event in the type of business in which the taxpayer is engaged. In certain types of business it is customary to eliminate unprofitable lines and add new lines as, for example, in a business the products of which are affected by style changes. Such variation in products would not qualify as a change in products furnished. The addition of a new product to a line of varied products, as where a novelty store selling hundreds of items adds several new lines, will not ordinarily be held to constitute the addition of new products for the purpose of section 443.

(2) The change in products or services furnished must take the form of the addition of a product or service which is new to the taxpayer. The discontinuance of a product or service previously furnished by the taxpayer is not a change in products or services for the purpose of section 443.

(b) *Qualifying taxable year under section 443.* The qualifying taxable year must be one of the three taxable years of the taxpayer immediately following the taxable year of the first change in products or services upon which the taxpayer relies, which change must have occurred during the last 36 months of the taxpayer's base period. The taxable year with respect to which the taxpayer claims qualification under section 443 (a) and § 40.443–1 must be the earliest year with respect to which the taxpayer meets the requirement of such sections. For the purpose of the requirement of section 443 (a) (2) and § 40.443–1 (a) (2) as to gross income or net income, if more than one substantial change in products or services occurred during the prescribed period, the gross income or net income attributable to such new products or services shall be aggregated in determining whether the amount attributable to new products or services exceeds the stated percentages of total gross income or total net income, as the case may be.

(c) *Average monthly excess profits net income.* For the purpose of the requirement of section 443 (a) (3) and § 40.443–1 (a) (3) the average monthly excess profits net income for the qualifying taxable year must exceed 125 percent of such average for the taxable years ending within the taxpayer's base period and ending prior to the taxable year in which occurred the first change in products or services upon which the taxpayer relies. For the purpose of this requirement, average monthly excess profits net income shall be computed for any taxable year by making the adjustments provided in section 433 (b) as though that section were applicable to all taxable years, and by dividing the excess profits net income so computed for the taxable year by the number of months in the taxable year. The average monthly excess profits net income for any period of two or more taxable years is determined by ascertaining the excess of the aggregate of the excess profits net income (computed by making the adjustments provided in section 433 (b) as though that section were applicable to all taxable years) for all taxable years within the period over the aggregate of any deficits in excess profits net income (similarly computed) for all taxable years within the period, and by dividing the excess so ascertained by the total number of months in the taxable years in the period. The average monthly excess profits net income determined for any period shall in no case be less than zero.

§ 40.443–3 *Computations*—(a) *Average base period net income.* The average base period net income determined under section 443 (b) is computed as follows:

(1) The amount of the total assets determined under section 442 (f) and under § 40.442–3 (d) (1) for the last day of the taxpayer's last taxable year ending before July 1, 1950, or for the last day of the first taxable year in which the taxpayer first meets the requirements of section 443 (a) and § 40.443–1, whichever day is later, is multiplied by the base period rate of return determined under section 447 for the taxpayer's industry classification. Under section 443 (c) the taxpayer's industry classification is the classification to which is attributable the largest amount of the taxpayer's gross receipts for the taxable year which includes the day for which the amount of the taxpayer's total assets was determined for the computation in the preceding sentence.

(2) The amount determined in subparagraph (1) of this paragraph is reduced by the total interest paid or incurred by the taxpayer for the 12 months ending with the day for which the taxpayer's total assets were determined for the purpose of subparagraph (1) of this paragraph.

(b) *Capital addition or reduction.* The base period capital addition computed under section 435 (f) is not available to a taxpayer computing its average base period net income under section 443. The net capital addition or reduction computed under section 435 (g), however, is applicable to such a taxpayer in accordance with the following modifications:

(1) If the taxable year in which the taxpayer first meets the requirements of section 443 (a) and § 40.443–1 is a year ending after June 30, 1950, no net capital addition or reduction will be applicable in computing the excess profits credit based on income for that taxable year.

(2) In determining the net capital addition or reduction under section 435 (g) for a taxable year subsequent to the taxable year in which the taxpayer first met the requirements of section 443 (a) and § 40.443–1, the day immediately following the taxable year in which such requirements were first met, if such taxable year ends after June 30, 1950, shall be used in lieu of the first day of the taxpayer's first taxable year ending after June 30, 1950, wherever the latter day is referred to in section 435 (g).

(c) *Definitions.* For the purpose of section 443—

(1) For definition of "total assets" see § 40.442–3 (d) (1).

(2) The term "gross receipts" means gross receipts as defined in section 435 (e) (5).

(3) For rules for determining when a taxpayer "commenced business," see § 40.445–1.

(4) The term "base period" means the base period as defined in section 435 (b).

(5) For definition of "interest," see § 40.442–3 (d) (5).

SEC. 444. AVERAGE BASE PERIOD NET INCOME—INCREASE IN CAPACITY FOR PRODUCTION OR OPERATION.

(a) *In general.* If a taxpayer which commenced business on or before the first day of its base period established that, during the 36-month period ending on the last day of its base period, there was an increase, as defined in subsection (b), in its capacity for production or operation, the taxpayer's average base period net income determined under this section shall be the amount computed under subsection (c).

(b) *Increase in capacity.* An increase in capacity for production or operation shall be deemed to have occurred, for the purposes of this section, if the taxpayer establishes that it made an addition or additions to its facilities (as defined in subsection (d)) or replaced all or a part of its existing facilities, and that:

(1) As a result of such additions or replacements, its capacity for production or operation on the last day of its base period was 200 per centum or more of its capacity for production or operation on the day prior to the beginning of such 36-month period, or

(2) (A) As a result of such additions or replacements, its capacity for production or operation on the last day of its base period was 150 per centum or more of its capacity for production or operation on the day prior to the beginning of such 36-month period, and (B) the adjusted basis for determining gain upon sale or exchange of its total facilities on the last day of its base period was 150 per centum or more of the adjusted basis for determining gain upon sale or exchange of its total facilities on the day prior to the beginning of such 36-month period, or

(3) The basis (unadjusted) for determining gain upon sale or exchange of its total facilities on the last day of its base period was 200 per centum or more of the basis (unadjusted) for determining gain upon sale or exchange of its total facilities on the day prior to the beginning of such 36-month period.

(c) *Average base period net income.* The average base period net income determined under this section shall be computed as follows:

(1) By multiplying the amount of the taxpayer's total assets for the last day of its taxable year immediately preceding its first taxable year under this subchapter by the base period rate of return, proclaimed by the Secretary under section 447, for the taxpayer's industry.

(2) By subtracting from the amount ascertained under paragraph (1) an amount equal to the total interest paid or incurred by the taxpayer for the 12 months ending with the end of such immediately preceding taxable year.

(d) *Facilities.* For the purposes of this section, the term "facilities" means real property and depreciable tangible property, held by the taxpayer in good faith for the purposes of the business.

(e) *Taxpayer's industry classification.* For the purposes of this section, the taxpayer's industry classification shall be the industry

classification under section 447 to which is attributable the largest amount of the taxpayer's gross receipts for its taxable year immediately preceding its first taxable year under this subchapter.

(f) *Rules for application of section.* The benefits of this section shall not be allowed unless the taxpayer makes application therefor in accordance with section 447 (e).

(g) *Cross references.* (1) For definition of gross receipts, see section 435 (e) (5).

(2) For definition of total assets, see section 442 (f).

(3) For computation of excess profits credit based on income in the case of certain reorganizations, see Part II of this subchapter.

§ 40.444–1 *Increase in capacity for production or operation.* A taxpayer may compute its average base period net income under section 444 if it commenced business on or before the first day of its base period and if it establishes that during the 36-month period ending on the last day of its base period there was an increase in its capacity for production or operation, as defined in section 444 (b). However, the benefits of section 444 are allowed only if the taxpayer makes application therefor in accordance with section 447 (e). For rules governing the application of section 444 in the case of an acquiring corporation, see section 462 (f), and in the case of a component corporation, see section 461 (c).

§ 40.444–2 *Requirements as to increase in capacity for production or operation*—(a) *Meaning of term "capacity for production or operation."* (1) As used in section 444, the term "capacity for production or operation" means the capacity to produce or to operate rather than the level of production or operation actually achieved. For example, a change from one shift to two shifts per day does not constitute an increase in capacity, but merely represents the utilization of existing capacity.

(2) The words "capacity for production or operation" shall be construed as alternatives, that is, capacity for production or capacity for operation. Thus, in the case of a manufacturer, an increase in the capacity for production may result from the acquisition of additional manufacturing facilities. In the case of a corporation engaged primarily in selling operations or the rendering of services, an increase in the capacity for operation may result from an increase in capacity to make sales or render services.

(3) For the purpose of section 444, an increase in capacity for production or operation must result either from an addition to or from a replacement of all or a part of the taxpayer's facilities, and must occur during the 36-month period ending on the last day of the taxpayer's base period.

(b) *Measurement of increase in capacity for production or operation.* (1) For the purpose of section 444, an increase in capacity for production or operation is deemed to have occurred if the taxpayer establishes that it made an addition or additions to its facilities or replaced all or a part of its existing facilities, and that—

(i) As a result of such addition or replacement, its capacity for production or operation on the last day of its base period was 200 percent or more of its total capacity for production or operation on the last day of the twelfth month of its base period, or

(ii) (*a*) As a result of such addition or replacement, its capacity for production or operation on the last day of its base period was 150 percent or more of its total capacity for production or operation on the last day of the twelfth month of its base period, and (*b*) the adjusted basis for determining gain upon sale or exchange of its total facilities on the last day of its base period was 150 percent or more of the adjusted basis for determining gain upon sale or exchange of its total facilities on the last day of the twelfth month of its base period, or

(iii) The basis (unadjusted) for determining gain upon sale or exchange of its total facilities on the last day of its base period was 200 percent or more of the basis (unadjusted) for determining gain upon sale or exchange of its total facilities on the last day of the twelfth month of its base period.

(2) In determining capacity for production or operation, the unit of measurement customary for the output of the particular kind of business shall be used, such as tons, gallons, barrels, yards, or dozens. In those businesses having no customary unit of measurement, an acceptable alternative might be expressed in terms of the principal raw material utilized. Dollar amounts may be used only if there is no other practical measurement for such output and then only if the taxpayer can establish that no distortion in the comparison results. The same unit of measurement must be used in computing capacity for the last day of the base period as is used in computing capacity for the last day of the twelfth month of the base period, except that the capacity for the last day of the base period must not include any increase not due to replacements or additions to facilities.

(3) For the purpose of subdivisions (ii) and (iii) of subparagraph (1) of this paragraph, the adjusted basis or the basis (unadjusted), as the case may be, of all facilities of the taxpayer is to be included in the computation for the last day of the twelfth month of the base period and in the computation for the last day of the base period, irrespective of whether the facility is one directly involved in any determination of capacity for production or operation.

§ 40.444–3 *Computations*—(a) *Average base period net income.* Average base period net income is computed under section 444 (c) as follows:

(1) The amount of the total assets determined under section 442 (f) and under § 40.442–3 (d) (1) for the last day of the taxpayer's last taxable year ending before July 1, 1950, is multiplied by the base period rate of return determined under section 447 for the taxpayer's industry classification. Under section 444 (e) the taxpayer's industry classification is the industry classification to which is attributable the largest amount of the taxpayer's gross receipts for its last taxable year ending before July 1, 1950.

(2) The amount ascertained under subparagraph (1) of this paragraph is reduced by the total interest paid or incurred by the taxpayer for the 12 months ending with the last day of the taxpayer's last taxable year ending before July 1, 1950.

(b) *Capital addition or reduction.* The base period capital addition computed under section 435 (f) is not available to a taxpayer computing its average base period net income under section 444. The net capital addition or reduction computed under section 435 (g), however, is applicable to such a taxpayer.

(c) *Definitions.* For the purpose of this section—

(1) For definition of "total assets," see § 40.442–3 (d) (1).

(2) The term "gross receipts" means gross receipts as defined in section 435 (e) (5).

(3) For rules for determining when a taxpayer "commenced business," see § 40.445–1.

(4) The term "base period" means the base period as defined in section 435 (b).

(5) The term "facilities" means tangible property of a character which is subject to the allowance for depreciation provided in section 23 (*l*) and real property, held by the taxpayer in good faith for the purposes of the business.

(6) For definition of "interest," see § 40.442–3 (d) (5).

SEC. 445. AVERAGE BASE PERIOD NET INCOME—NEW CORPORATION.

(a) *New corporation.* A taxpayer which commenced business after the first day of its base period shall, except as provided in subsection (g), be considered a new corporation for the purposes of this section, and its average base period net income determined under this section shall be the amount computed under subsection (b).

(b) *Average base period net income.* The average base period net income of a new corporation determined under this section shall be computed as follows:

(1) For the purpose of determining the excess profits credit for any of the taxpayer's first three taxable years which is a taxable year under this subchapter—

(A) By multiplying the amount of the total assets for such taxable year (determined under subsection (c)), held by the taxpayer in good faith for the purposes of the business, by the base period rate of return, proclaimed by the Secretary under section 447, for the taxpayer's industry classification.

(B) By subtracting from the amount ascertained under subparagraph (A) the total interest paid or incurred by the taxpayer for the 12 months ending with the last day of such taxable year.

(2) For the purpose of determining the excess profits credit for any taxable year under this subchapter other than a taxable year described in paragraph (1)—

(A) By multiplying the amount of the taxpayer's total assets (as defined in section 442 (f)) for (i) the last day of its taxable year immediately preceding its first taxable year under this subchapter, or (ii) the last day of its third taxable year, whichever day is later, by the base period rate of return, proclaimed by the Secretary under section 447, for the taxpayer's industry classification.

(B) By subtracting from the amount ascertained under subparagraph (A) the total interest paid or incurred by the taxpayer for the 12 months ending with whichever day is used under such subparagraph.

For the purposes of this section, the taxable year of the taxpayer in which it commenced business and its two succeeding taxable

years shall be considered to be its first three taxable years.

(c) *Total assets for first three years.* The amount of the total assets for any taxable year referred to in subsection (b) (1) shall, for the purposes of such subsection, be the sum of

(1) The total assets (as defined in section 442 (f)) for the last day of the taxpayer's taxable year immediately preceding its first taxable year under this subchapter, and

(2) The net capital addition (determined under section 435 (g)) for such taxable year referred to in subsection (b) (1),

minus the net capital reduction (determined under section 435 (g) for such taxable year referred to in subsection (b) (1).

(d) *Taxpayer's industry classification.* The taxpayer's industry classification shall be determined, for the purposes of subsection (b) (1), by reference to the particular taxable year for which the excess profits credit is thereunder determined, and, for the purposes of subsection (b) (2), by reference to the taxpayer's third taxable year; and, in either case, shall be the industry classification under section 447 to which is attributable the largest amount of the taxpayer's gross receipts for such taxable year.

(e) *Capital addition or reduction.* If the average base period net income of the taxpayer is determined under this section—

(1) The excess profits credit for any taxable year for which such determination is made under subsection (b) (1) shall not include any net capital addition or reduction determined under section 435 (g), and

(2) In computing the net capital addition or reduction under section 435 (g) for any taxable year for which such determination is made under subsection (b) (2), the expression "the first day of the taxpayer's first taxable year under this subchapter" shall be read as "the first day of the taxpayer's first taxable year under this subchapter or the day following the close of the taxpayer's third taxable year, whichever day is later."

(f) *Rules for application of section.* The benefits of this section shall not be allowed unless the taxpayer makes application therefor in accordance with section 447 (e).

(g) *Ineligible corporations.* (1) If a taxpayer, on or after December 1, 1950, and prior to the end of its third taxable year, acquires any properties in any of the transactions described in paragraph (2), it shall not, for the taxable year in which such acquisition occurs or for succeeding taxable years, be entitled to the benefits of this section except under the circumstances and subject to the limitations provided in section 462 (g).

(2) The transactions to which paragraph (1) applies are as follows:

(A) The acquisition by the taxpayer from another corporation of properties the basis of which in its hands is determined by reference to the basis of such properties to the transferor;

(B) The acquisition by the taxpayer of a substantial part of its assets from another corporation, or of a substantial part of the properties of another corporation, if 50 per centum or more in value of the outstanding stock or outstanding voting stock of the taxpayer is directly or indirectly owned, at the time of such acquisition, by individuals owning directly or indirectly 50 per centum or more in value of the outstanding stock, or outstanding voting stock of the transferor;

(C) The acquisition by the taxpayer of a substantial part of the properties distributed on or after December 1, 1950, by another corporation, if such properties constituted a substantial part of the business assets of such other corporation, and if 50 per centum or more in value of the outstanding stock or outstanding voting stock of the taxpayer is owned directly or indirectly by individuals who at the time of such distribution owned directly or indirectly 50 per centum or more in value of the outstanding stock or outstanding voting stock of such other corporation;

(3) For the purposes of this subsection, the provisions of section 503 shall be applicable in the determination of ownership of stock.

(h) *Cross references.* (1) For definition of gross receipts, see section 435 (e) (5).

(2) For computation of excess profits credit based on income in the case of certain reorganizations, see Part II of this subchapter.

§ 40.445–1 *New corporations*—(a) *In general.* (1) Section 445 provides an alternative average base period net income for new corporations. For the purpose of section 445 and the regulations thereunder, a taxpayer which commenced business after the first day of its base period and which is not an ineligible corporation is considered to be a new corporation. However, section 445 is applicable only if the taxpayer makes application therefor in accordance with section 447 (e). For rules governing the application of section 445 in the case of an acquiring corporation, see section 462 (g), and in the case of a component corporation, see section 461 (c).

(2) The words "commenced business" do not have the same meaning as "in existence." Ordinarily, a corporation commences business when it starts the business operations for which it was organized; a corporation comes into existence on the date of its incorporation. Mere organizational activities, such as incorporation or the issuance of capital stock, are not alone sufficient to show commencement of business. If the activities of the corporation have advanced to the extent necessary to establish the nature of its business operations, it will be deemed to have commenced business. For example, the acquisition of operating assets which are necessary to the type of business contemplated may constitute the commencement of business.

(b) *Ineligible corporations.* If a taxpayer, on or after December 1, 1950, and prior to the end of its third taxable year (counting as the first taxable year, the taxable year in which the taxpayer commenced business), acquires any properties in any of the transactions described in subparagraphs (1), (2), or (3) of this paragraph, it shall be deemed an "ineligible corporation" and it shall not be entitled to the application of section 445 for the taxable year in which such acquisition occurs or for any succeeding taxable year, except under the circumstances and subject to the limitations provided in section 462 (g). The transactions referred to above are—

(1) The acquisition by the taxpayer from another corporation of properties the basis of which in the hands of the taxpayer is determined by reference to the basis of such properties to the transferor; or

(2) The acquisition by the taxpayer of a substantial part of its assets from another corporation, or of a substantial part of the properties of another corporation, if 50 percent or more in value of the outstanding stock or outstanding voting stock of the taxpayer is directly or indirectly owned, at the time of such acquisition, by individuals owning directly or indirectly 50 percent or more in value of the outstanding stock, or outstanding voting stock of the transferor; or

(3) The acquisition by the taxpayer of a substantial part of the properties distributed on or after December 1, 1950, by another corporation, if such properties constituted a substantial part of the business assets of such other corporation, and if 50 percent or more in value of the outstanding stock or outstanding voting stock of the taxpayer is owned directly or indirectly by individuals who at the time of such distribution owned directly or indirectly 50 percent or more in value (g), and in the case of a component voting stock of such corporation.

(c) For the purpose of paragraph (b) of this section, the provisions of section 503 are applicable in determining the ownership of stock.

§ 40.445–2 *Computations*—(a) *Average base period net income for first three taxable years.* The average base period net income for each of the taxpayer's first three taxable years (counting as the first taxable year, the taxable year in which the taxpayer commenced business) which is an excess profits tax taxable year is computed under section 445 as follows:

(1) The amount of the taxpayer's total assets determined under paragraph (d) (1) of this section for such taxable year is multiplied by the base period rate of return determined under section 447 for the taxpayer's industry classification. Under section 445 (d), the taxpayer's industry classification is the classification to which is attributable the largest amount of the taxpayer's gross receipts for the taxable year for which the excess profits credit is being determined.

(2) The amount ascertained under subparagraph (1) of this paragraph is reduced by the total interest paid or incurred by the taxpayer for the 12 months ending with the last day of the taxable year for which the excess profits credit is being determined.

(b) *Average base period net income for fourth and subsequent taxable years.* The average base period net income for each excess profits tax taxable year subsequent to the taxpayer's third taxable year (counting as the first taxable year, the taxable year in which the taxpayer commenced business) is computed under section 445 as follows:

(1) The amount of the taxpayer's total assets determined under paragraph (d) (2) of this section is multiplied by the base period rate of return determined under section 447 for the taxpayer's industry classification. Under section 445 (d), the taxpayer's industry classification is the classification to which is attributable the largest amount of the taxpayer's gross receipts for its third taxable year.

(2) The amount ascertained under subparagraph (1) of this paragraph is reduced by the total interest paid or incurred by the taxpayer for the 12 months ending with the day for which the taxpayer's total assets are computed under paragraph (d) (2) of this section.

(c) *Capital addition or reduction.* The base period capital addition computed under section 435 (f) is not avail-

able to a taxpayer computing its average base period net income under section 445. The net capital addition or reduction computed under section 435 (g) is, however, applicable to such a taxpayer in accordance with the following modifications:

(1) In the case of a taxpayer computing its average base period net income under section 445 (b) (1) and under paragraph (a) of this section for any of its first three taxable years, the net capital addition or reduction is not applicable. See, however, paragraph (d) (1) of this section for inclusion of net capital addition or reduction in determining total assets.

(2) In the case of a taxpayer computing its average base period net income under section 445 (b) (2) and under paragraph (b) of this section for its fourth taxable year, or for any taxable year subsequent thereto, the net capital addition or reduction is applicable. However, if the taxpayer's third taxable year ends after June 30, 1950, then the day following the close of such taxable year shall be used in lieu of the first day of the taxpayer's first taxable year ending after June 30, 1950, wherever the latter day is referred to in section 435 (g).

(d) *Definitions.* For the purpose of this section—

(1) The amount of the taxpayer's "total assets" for any taxable year referred to in paragraph (a) of this section, is (i) the sum of (a) the total assets (as defined in section 442 (f) and §40.442–3 (d) (1)) for the last day of the taxpayer's last taxable year ending before July 1, 1950, and (b) the net capital addition determined under section 435 (g) for the taxable year for which the excess profits credit is being computed, minus (ii) the net capital reduction determined under section 435 (g) for such taxable year. If the taxpayer's first taxable year ended after June 30, 1950, its total assets consist only of its net capital addition for the taxable year for which the excess profits credit is being computed.

(2) The amount of the taxpayer's "total assets" for any taxable year referred to in paragraph (b) of this section, means the total assets determined under section 442 (f) and § 40.442–3 (d) (1) for the last day of the taxpayer's last taxable year ending before July 1, 1950, or the last day of the taxpayer's third taxable year, whichever day is later.

(3) The term "gross receipts" means gross receipts as defined in section 435 (e) (5).

(4) The term "base period" means the base period as defined in section 435 (b).

(5) For the purpose of this section, the taxable year of the taxpayer in which it commenced business and its two immediately succeeding taxable years shall be considered to be its first three taxable years.

(6) For definition of "interest" see § 40.442–3 (d) (5).

SEC. 446. AVERAGE BASE PERIOD NET INCOME—DEPRESSED INDUSTRY SUBGROUPS.

(a) *In general.* If a taxpayer which commenced business on or before the first day of its base period is a member of a depressed industry subgroup, as defined in subsection (c), its average base period net income determined under this section shall be the amount computed under subsection (b).

(b) *Average base period net income.* The average base period net income determined under this section shall be computed as follows:

(1) By determining the amount of the taxpayer's total assets for the last day of each of its taxable years ending after the first day of its base period and prior to the first day of its first taxable year under this subchapter.

(2) By computing the average of the amounts ascertained under paragraph (1).

(3) By multiplying the amount ascertained under paragraph (2) by the adjusted rate of return, proclaimed by the Secretary under subsection (e), for the taxpayer's industry subgroup.

(4) By determining the aggregate amount of interest paid or incurred by the taxpayer for all taxable years ending after the first day of its base period and prior to the first day of its first taxable year under this subchapter, dividing such aggregate by the total number of months in such years, and multiplying the quotient by 12.

(5) By subtracting the amount ascertained under paragraph (4) from the amount ascertained under paragraph (3).

(c) *Depressed industry subgroups.* The Secretary shall determine and proclaim as a depressed industry subgroup any industry subgroup (defined in accordance with subsection (f) having a rate of return (determined under subsection (d) (1)) for the period 1946 through 1948 which is less than 63 per centum of its rate of return (determined under subsection (d) (2)) for the period 1938 through 1948.

(d) *Rates of return for industry subgroups*—(1) *Period 1946–48.* The rate of return for an industry subgroup for the 3-year period 1946 through 1948 shall be obtained by dividing the sum of the aggregate net income (computed without regard to the net operating loss deduction provided in section 23 (s)) for the 3 years 1946 through 1948 and the aggregate interest deduction for such years shown on the income tax returns filed by the corporations in such industry subgroup submitting balance sheets, by the aggregate assets for such years of such corporations as of the close of the taxable years for which such returns were filed. Such aggregate net income, interest deduction and total assets shall include the amounts reported on the income tax returns for the calendar years 1946, 1947, and 1948, and the amounts reported on returns for other taxable years the greater part of which falls in such calendar years.

(2) *Period 1938–48.* The rate of return for an industry subgroup for the 11-year period 1938 through 1948 shall be determined in the same manner as is provided in paragraph (1) with the substitution of the years 1938 through 1948 for the years 1946 through 1948.

(e) *Adjusted rates of return for depressed industry subgroups.* The adjusted rate of return for a depressed industry subgroup shall be a rate equal to four-fifths of the rate of return for such industry subgroup for the 11-year period 1938 through 1948 as determined under subsection (d) (2). The Secretary shall determine and proclaim the adjusted rate of return (computed to the nearest thousandth) for each industry subgroup determined and proclaimed to be depressed under subsection (c).

(f) *Industry subgroups.* For the purposes of this section, industry subgroups shall be generally in accord with the industry subgroups regularly used by the Treasury Department in compiling published statistics from income tax returns, but with such combinations of subgroups as the Secretary determines are necessary to provide reasonably comparable data over the period 1938 through 1948.

(g) *Members of industry subgroup.* For the purposes of this section, a taxpayer is a member of an industry subgroup if more than fifty per centum of the taxpayer's gross receipts (as defined in section 435 (e) (5)) for the taxable years beginning with or within its base period is attributable to such industry subgroup.

(h) *Tentative determinations of depressed industry subgroups and adjusted rates of return.* The Secretary, not later than March 1, 1951, shall proclaim the industry subgroups tentatively determined to be depressed in accordance with subsection (c) and the tentative adjusted rates of return (computed to the nearest thousandth), determined under subsection (d), for such industry subgroups. Such tentative determinations shall be effective until such time as final determinations are proclaimed by the Secretary. Such final determinations shall relate back as though such determinations had been in effect in place of the tentative determinations. If the application of this section is made in accordance with a tentative determination, such application shall be redetermined in accordance with the final determination when proclaimed. The period of limitation prescribed under sections 275, 276, and 322 shall not begin to run with respect to overpayments or deficiencies in tax caused by such redetermination prior to such time as the final determination is proclaimed by the Secretary.

(i) *Rules for application of section.* The benefits of this section shall not be allowed unless the taxpayer makes application therefor in accordance with section 447 (e). The determinations by the Secretary required under this section shall be made on the basis of returns regularly used by the Treasury Department in compiling published statistics from income tax returns. For the purposes of this section, rates of return shall be determined after giving effect to renegotiation of contracts in accordance with renegotiation statistics published in the statistics compiled with respect to industry subgroups.

§ 40.446–1 *General rule.* A taxpayer which commenced business on or before the first day of its base period and which is a member of a depressed industry subgroup may be entitled to use the average base period net income computed under section 446. See § 40.446–3, for method of computation. However, section 446 is applicable only if the taxpayer makes application therefor in accordance with section 447 (e). For rules governing application of section 446 in the case of an acquiring corporation, see section 462 (h), and in the case of a component corporation, see section 461 (c). For the purpose of section 446, a taxpayer is a member of a depressed industry subgroup if more than 50 percent of the aggregate of its gross receipts for all of the taxable years beginning with or within its base period is attributable to such depressed industry subgroup.

§ 40.446–2 *Determination of depressed industry subgroups and adjusted rates of return therefor.* (a) For the purpose of section 446, the depressed industry subgroups determined and proclaimed to be depressed by the Secretary are defined in accordance with specifications shown in the Standard Industrial Classification Manual prepared by the Division of Statistical Standards, Bureau of the Budget.

(b) For the purpose of section 446, depressed industry subgroups and adjusted rates of return for depressed industry subgroups are only those proclaimed by the Secretary. Under section

446 (h), tentative determinations of depressed industry subgroups and adjusted rates of return have been proclaimed by the Secretary, and are set forth below. The tentative adjusted rates of return and tentative determinations of depressed industry subgroups shall be effective until such time as the adjusted rates described in section 446 (e) and the determinations of depressed industry subgroups under section 446 (c) are determined and proclaimed by the Secretary. The adjusted rates of return, when proclaimed by the Secretary, shall relate back as though they had been in effect in place of the tentative adjusted rates. Any application of section 446 made in accordance with a tentative determination and tentative adjusted rate shall be redetermined in accordance with the final determination and adjusted rate when proclaimed. The period of limitations prescribed under section 322 and sections 275 and 276 with respect to overpayments or deficiencies in tax caused by such redetermination shall not begin to run prior to the time that the adjusted rates of return are determined and proclaimed.

(c) The tentative determinations of depressed industry subgroups and the tentative adjusted rates of return therefor are as follows:

| *Industry subgroup* | *Tentative-adjusted rate of return (percent)* |
|---|---|
| 1. The manufacture of aircraft and parts, including aircraft engines | 11.3 |
| This industry subgroup is Standard Industrial Classification No. 372,[1] consisting of the following: 3721 (Aircraft), 3722 (Aircraft engines and engine parts), 3723 (Aircraft propellers and propeller parts), and 3729 (Aircraft parts and auxiliary equipment, not elsewhere classified). | |
| 2. The manufacture of engines and turbines, except automotive, aircraft and railway | 12.8 |
| This industry subgroup is Standard Industrial Classification No. 351,[1] consisting of the following: 3511 (Steam engines, turbines, and water wheels), and 3519 (Diesel and semi-Diesel engines; and other internal-combustion engines, not elsewhere classified). | |
| 3. The manufacture of metalworking machinery, including machine tools | 16.8 |
| This industry subgroup is Standard Industrial Classification No. 354,[1] consisting of the following: 3541 (Machine tools), 3542 (metalworking machinery, except machine tools), and 3543 (Machine tool accessories and other metalworking machinery; small power-driven cutting and shaping tools and tool holders; and precision measuring tools). | |
| 4. Ship and boat building and repairing | 10.4 |
| This industry subgroup is Standard Industrial Classification No. 373,[1] consisting of the following: 3731 (Ship building and repairing), and 3732 (Boat building and repairing). | |
| 5. The manufacture of wines | 7.8 |
| This industry subgroup is Standard Industrial Classification No. 2084[1] (Wines). | |
| 6. Photographic studios, including commercial photography | 8.6 |
| This industry subgroup is Standard Industrial Classification No. 723,[1] consisting of the following: 7231 (Photographic studios, except commercial photography), and 7232 (Commercial photography). | |
| 7. Telegraphic communication, wire and radio | 1.5 |
| This industry subgroup is Standard Industrial Classification No. 4821[1] (Telegraphic communication, wire and radio). | |
| 8. Transportation by air | 3.0 |
| This industry subgroup is Standard Industrial Classification No. 45,[1] consisting of the following: 4512 (Certified carriers), 4513 (Uncertified carriers), 4521 (Air carriage, except common carriers), 4582 (Airports and flying fields), and 4583 (Airport terminal services). | |

[1] References are to the Standard Industrial Classification Manual prepared by the Division of Statistical Standards, Bureau of the Budget.

§ 40.446–3 *Computations*—(a) *Average base period net income.* The computation of the average base period net income under section 446 (b) is as follows:

(1) The amount of the taxpayer's total assets for the last day of each taxable year ending after the first day of its base period and prior to July 1, 1950, is determined under section 442 (f) and under § 40.442–3 (d) (1).

(2) The sum of the amounts ascertained under subparagraph (1) of this paragraph is divided by the number of such amounts.

(3) The average ascertained under subparagraph (2) of this paragraph is multiplied by the adjusted rate of return for the taxpayer's industry subgroup. Under section 446 (g) and § 40.446–2, the taxpayer's industry subgroup is the industry subgroup to which is attributable more than 50 percent of the aggregate of the taxpayer's gross receipts for all of the taxable years beginning with or within its base period.

(4) The average of the aggregate interest paid or incurred by the taxpayer for all taxable years ending after the first day of its base period and prior to July 1, 1950, is subtracted from the amount determined under subparagraph (3) of this paragraph. This average is computed by ascertaining the total of such interest for all such taxable years, by dividing the amount so ascertained by the number of months in such taxable years, and by multiplying the quotient by 12.

(b) *Capital addition or reduction.* The base period capital addition determined under section 435 (f) is not available to a taxpayer computing its average base period net income under section 446. The net capital addition or reduction, computed under section 435 (g), however, is applicable to such a taxpayer.

(c) *Definitions.* For the purpose of this section:

(1) For definition of "total assets," see § 40.442–3 (d) (1).

(2) The term "gross receipts" means gross receipts as defined in section 435 (e) (5).

(3) For rules for determining when a taxpayer "commenced business," see § 40.445–1.

(4) The term "base period" means the base period as defined in section 435 (b).

(5) For definition of "interest," see § 40.442–3 (d) (5).

SEC. 447. INDUSTRY BASE PERIOD RATES OF RETURN.

(a) *Base period yearly rate of return.* The Secretary shall determine and proclaim for each industry classification in subsection (c) a rate of return (computed to the nearest thousandth) for each of the four years 1946 through 1949. The yearly rate of return for each industry classification shall be obtained by dividing the sum of the aggregate net income (computed without regard to the net operating loss deduction provided in section 23 (s)) and the aggregate interest deduction shown on the income tax returns filed by the corporations in such classification submitting balance sheets, by the aggregate total assets of such corporations as of the close of the taxable year for which such returns were filed. Such aggregate net income, interest deduction and total assets for each such year shall include the amounts reported on the income tax returns for the calendar year and the amounts reported on returns for other taxable years the greater part of which falls in such calendar year. The determinations by the Secretary required under this section shall be made on the basis of returns regularly used by the Treasury Department in compiling published statistics from income tax returns, computing all rates of return after giving effect to renegotiation of contracts in accordance with renegotiation statistics published in the statistics compiled with respect to industry classifications.

(b) *Base period rate of return.* The Secretary shall determine and proclaim for each industry classification in subsection (c) a rate of return (computed to the nearest thousandth) for the four-year period 1946 through 1949. Such base period rate of return for each industry classification shall be obtained by aggregating the net income and interest deduction (such amounts being determined as provided under subsection (a)) for such four years and dividing the aggregate by the sum of the total assets (determined as provided under subsection (a)) for such four years.

(c) *Industry classification.* For purposes of this subchapter the classification of taxpayers by industry shall be as provided in the table below. Each such industry classification is defined in accordance with the specifications shown in the Standard Industrial Classification Manual (prepared by the Division of Statistical Standards, Bureau of the Budget) for the major industry group or groups the numbers of which appear opposite such classification.

INDUSTRY CLASSIFICATIONS

| | *Major group No.* |
|---|---|
| *Agriculture, Forestry, and Fisheries* | |
| Farms and agricultural services, hunting, trapping | 01 and 07 |
| Forestry | 08 |
| Fisheries | 09 |
| *Mining* | |
| Metal mining | 10 |
| Anthracite mining | 11 |
| Bituminous coal and lignite mining | 12 |
| Crude petroleum and natural gas extraction | 13 |
| Nonmetallic minerals except fuels | 14 |
| *Contract Construction* | |
| General contractors | 15 and 16 |
| Special trade contractors | 17 |
| *Manufacturing* | |
| Ordnance and accessories | 19 |
| Food and kindred products | 20 |
| Tobacco manufactures | 21 |
| Textile mill products | 22 |

INDUSTRY CLASSIFICATIONS—Continued

*Manufacturing*—Continued

| | Major group No. |
|---|---|
| Apparel and other finished products made from fabrics | 23 |
| Lumber and wood products | 24 |
| Furniture and fixtures | 25 |
| Paper and allied products | 26 |
| Printing, publishing, and allied industries | 27 |
| Chemicals and allied products | 28 |
| Products of petroleum and coal | 29 |
| Rubber products | 30 |
| Leather and leather products | 31 |
| Stone, clay, and glass products | 32 |
| Primary metal industries and fabricated metal products (except ordnance, machinery, and transportation equipment) | 33 and 34 |
| Machinery (except electrical) | 35 |
| Electrical machinery, equipment, and supplies | 36 |
| Transportation equipment | 37 |
| Professional, scientific, and controlling instruments; photographic and optical goods; watches and clocks; including miscellaneous manufacturing industries | 38 and 39 |

*Transportation, Communication, and Other Public Utilities*

| | |
|---|---|
| Railroads | 40 |
| Local and interurban railways and bus lines | 41 |
| Trucking and warehousing | 42 |
| Highway transportation not elsewhere classified | 43 |
| Water transportation | 44 |
| Transportation by air | 45 |
| Pipe line transportation | 46 |
| Services incidental to transportation | 47 |
| Telecommunications | 48 |
| Utilities and sanitary services | 49 |

*Wholesale Trade*

| | |
|---|---|
| Wholesale trade | 50 and 51 |

*Retail Trade*

| | |
|---|---|
| Building materials and farm equipment | 52 |
| General merchandise | 53 |
| Food | 54 |
| Automotive dealers and gasoline service stations | 55 |
| Apparel and accessories | 56 |
| Furniture, home furnishings, and equipment | 57 |
| Eating and drinking places | 58 |
| Miscellaneous retail stores | 59 |

*Finance, Insurance, and Real Estate*

| | |
|---|---|
| Banking | 60 |
| Credit agencies other than banks | 61 |
| Security and commodity brokers, dealers, exchanges, and services | 62 |
| Insurance carriers | 63 |
| Insurance agents, brokers, and service | 64 |
| Real estate | 65 |
| Holding and other investment companies | 67 |

*Services*

| | |
|---|---|
| Hotels, rooming houses, camps, and other lodging places | 70 |
| Personal services | 72 |
| Miscellaneous business services | 73 |
| Automobile repair services and garages | 75 |
| Miscellaneous repair services | 76 |
| Radio broadcasting, including facsimile broadcasting, and television | 77 |
| Motion pictures | 78 |
| Amusement and recreation services except motion pictures | 79 |
| Other services | 80, 81, 82, 84, 86, and 89 |

(d) *Tentative rates of return.* The Secretary, not later than March 1, 1951, shall determine and proclaim for each industry classification, tentative base period yearly rates of return and a tentative base period rate of return (each computed to the nearest thousandth). Such tentative rates of return shall be effective until such time as the base period yearly rates of return and base period rates of return are determined and proclaimed. The base period yearly rates of return and base period rates of return, upon proclamation thereof by the Secretary, shall relate back as though such rates had been in effect in place of the tentative rates of return. If the application of section 442, 443, 444, 445, or 446 is made in accordance with tentative rates of return, such application shall be redetermined in accordance with the base period yearly rate of return or the base period rate of return when determined and proclaimed. The period of limitation prescribed under section 322 and sections 275 and 276 shall not begin to run with respect to overpayments or deficiencies in tax caused by such redetermination prior to such time as the base period yearly rates of return and the base period rates of return are determined and proclaimed by the Secretary.

(e) *Application for benefits of section 442, 443, 444, 445, or 446.* The tax for any taxable year under this subchapter shall be determined without regard to section 442, 443, 444, 445, or 446 unless an application for the benefits of such section, setting forth the grounds for the application of such section in such detail and in such manner as the Secretary may prescribe, is filed by the taxpayer—

(A) With its return for the taxable year, or

(B) Within the period of time prescribed by section 322 (as extended under the last sentence of subsection (d) of this section or of section 446 (h)) for filing claim for credit or refund, and in such case the application of section 442, 443, 444, 445, or 446, shall be subject to the limitations as to amount of credit or refund prescribed in section 322, or

(C) After the period described in paragraph (B), if within the period of limitations for the assessment of a deficiency (as extended under the last sentence of subsection (d) of this section or of section 446 (h)) in the tax imposed by this chapter for the taxable year, and in such case the application of section 442, 443, 444, 445, or 446 shall not reduce the tax by an amount greater than the deficiency determined without regard to the application of such section,

except that if a petition is filed with the Tax Court for the redetermination of the tax under this chapter for the taxable year, the application for the benefits of section 442, 443, 444, 445, or 446, shall be effective only if filed not later than the date on which such petition is filed. Section 442, 443, 444, 445, or 446, shall not be applied upon the basis of any grounds other than those set forth in an application filed within the period prescribed in this subsection.

§ 40.447–1 *Industry base period rates of return*—(a) *In general.* Sections 442 through 445 provide for the determination of an average base period net income computed, in general, on the basis of an industry rate of return determined under section 447 rather than on the basis of the taxpayer's own experience. Section 447 provides for two types of industry rates of return. The first, for use under section 442 (c) (relating to 12 or fewer months affected by abnormalities) is designated as the base period yearly rate of return. The second, for use under sections 442 (d), 443, 444, or 445, is designated as the base period rate of return.

(b) *Industry classification.* For the purpose of sections 442 through 445, and of section 447, the industry classification must be one set forth in section 447 (c). Each industry classification set forth in section 447 (c) is defined in accordance with the specifications shown in the Standard Industrial Classification Manual prepared by the Division of Statistical Standards of the Bureau of the Budget. The industry classification of the taxpayer is to be determined in accordance with the specifications shown in that manual.

(c) For the purpose of sections 442 through 445, and of section 447, the base period yearly rates of return and the base period rates of return are only those rates of return which are proclaimed by the Secretary. Under section 447 (d), tentative base period yearly rates of return and tentative base period rates of return have been proclaimed by the Secretary, and are set forth in § 40.447–2. These tentative rates shall be effective until such time as the rates described in section 447 (a) and (b) are determined and proclaimed by the Secretary. The rates described in section 447 (a) and (b), when proclaimed by the Secretary, shall relate back as though they had been in effect in place of the tentative rates.

(d) Any application of sections 442 through 445 made in accordance with the tentative rates shall be redetermined in accordance with the final rates when proclaimed. The period of limitation prescribed under section 322 and sections 275 and 276 with respect to overpayments of or deficiencies in tax caused by such redetermination shall not begin to run prior to the time that the final rates of return under section 447 (a) and (b) are determined and proclaimed.

§ 40.447–2 *Tentative industry base period rates of return.* The industry classifications set forth in section 447 (c), and the tentative base period yearly rates of return and the tentative base period rate of return for each such industry classification are as follows:

| Major group number | Industry classification | Tentative base period yearly rates of return (percent) | | | | Tentative base period rate of return (percent) |
|---|---|---|---|---|---|---|
| | | 1946 | 1947 | 1948 | 1949 | |
| | *Agriculture, forestry, and fisheries* | | | | | |
| 01 and 07 | Farms and agricultural services, hunting, trapping | 12.5 | 12.8 | 12.7 | 11.9 | 12.5 |
| 08 | Forestry | 6.1 | 8.2 | 9.2 | 10.7 | 8.5 |
| 09 | Fisheries | 9.1 | 2.1 | 4.5 | 4.5 | 4.8 |
| | *Mining* | | | | | |
| 10 | Metal mining | 5.2 | 11.8 | 13.8 | 8.7 | 10.1 |
| 11 | Anthracite mining | 6.4 | 5.8 | 8.0 | 4.5 | 6.2 |
| 12 | Bituminous coal and lignite mining | 6.3 | 14.6 | 15.4 | 7.7 | 11.3 |
| 13 | Crude petroleum and natural gas extraction | 5.1 | 9.7 | 11.8 | 11.2 | 10.0 |
| 14 | Nonmetallic minerals except fuels | 11.9 | 14.2 | 15.0 | 14.9 | 14.2 |

| Major group number | Industry classification | Tentative base period yearly rates of return (percent) | | | | Tentative base period rate of return (percent) |
|---|---|---|---|---|---|---|
| | | 1946 | 1947 | 1948 | 1949 | |
| | *Contract construction* | | | | | |
| 15 and 16 | General contractors | 8.6 | 10.5 | 13.7 | 14.5 | 12.2 |
| 17 | Special trade contractors | 12.6 | 15.2 | 15.1 | 9.7 | 13.1 |
| | *Manufacturing* | | | | | |
| 19 | Ordnance and accessories | 4.5 | 11.6 | 14.8 | 7.1 | 9.4 |
| 20 | Food and kindred products | 18.4 | 15.2 | 12.4 | 13.2 | 14.6 |
| 21 | Tobacco manufactures | 9.7 | 9.8 | 11.1 | 11.8 | 10.7 |
| 22 | Textile mill products | 24.0 | 23.2 | 20.6 | 10.3 | 19.2 |
| 23 | Apparel and other finished products made from fabrics. | 21.8 | 16.7 | 10.4 | 8.0 | 13.8 |
| 24 | Lumber and wood products | 16.0 | 23.0 | 19.6 | 11.5 | 17.5 |
| 25 | Furniture and fixtures | 16.4 | 16.4 | 14.6 | 13.7 | 15.3 |
| 26 | Paper and allied products | 17.8 | 23.2 | 18.1 | 13.7 | 18.1 |
| 27 | Printing, publishing, and allied industries | 18.6 | 15.7 | 13.8 | 13.2 | 15.1 |
| 28 | Chemicals and allied products | 17.3 | 17.6 | 16.2 | 15.8 | 16.7 |
| 29 | Products of petroleum and coal | 6.1 | 8.7 | 11.3 | 6.6 | 8.3 |
| 30 | Rubber products | 18.6 | 12.4 | 13.4 | 9.0 | 13.2 |
| 31 | Leather and leather products | 19.3 | 15.9 | 10.2 | 8.3 | 13.3 |
| 32 | Stone, clay, and glass products | 15.4 | 16.3 | 17.2 | 16.8 | 16.5 |
| 33 and 34 | Primary metal industries and fabricated metal products (except ordnance, machinery, and transportation equipment). | 9.8 | 15.4 | 16.4 | 12.9 | 13.8 |
| 35 | Machinery (except electrical) | 9.4 | 16.0 | 17.2 | 14.7 | 14.6 |
| 36 | Electrical machinery, equipment, and supplies | 4.2 | 14.5 | 15.6 | 13.6 | 12.4 |
| 37 | Transportation equipment | 1.4 | 13.5 | 18.6 | 21.4 | 14.5 |
| 38 and 39 | Professional, scientific, and controlling instruments; photographic and optical goods; watches and clocks including miscellaneous manufacturing industries. | 11.9 | 13.8 | 13.5 | 12.8 | 13.0 |
| | *Transportation, communication, and other public utilities* | | | | | |
| 40 | Railroads | 2.1 | 3.9 | 5.3 | 4.0 | 3.9 |
| 41 | Local and interurban railways and bus lines | 4.1 | [1] (2.9) | 2.2 | 1.7 | 1.4 |
| 42 | Trucking and warehousing | 11.4 | 12.2 | 14.0 | 12.7 | 12.7 |
| 43 | Highway transportation not elsewhere classified | 24.1 | 15.1 | 12.1 | 10.4 | 15.2 |
| 44 | Water transportation | 9.1 | 9.9 | 8.1 | 8.4 | 8.9 |
| 45 | Transportation by air | [1] (2.6) | [1] (3.7) | 1.3 | 4.3 | .2 |
| 46 | Pipe line transportation | 11.1 | 10.5 | 10.5 | 9.1 | 10.1 |
| 47 | Services incidental to transportation | 8.1 | 10.0 | 7.1 | 7.2 | 8.1 |
| 48 | Telecommunications | 6.1 | 4.1 | 4.9 | 5.0 | 5.0 |
| 49 | Utilities and sanitary services | 7.0 | 6.3 | 6.1 | 6.5 | 6.4 |
| | *Wholesale trade* | | | | | |
| 50 and 51 | Wholesale trade | 16.5 | 15.3 | 12.6 | 9.7 | 13.3 |
| | *Retail trade* | | | | | |
| 52 | Building materials and farm equipment | 15.3 | 16.3 | 15.3 | 10.0 | 14.3 |
| 53 | General merchandise | 20.9 | 17.4 | 16.7 | 13.2 | 16.9 |
| 54 | Food | 15.8 | 13.9 | 12.9 | 15.8 | 14.6 |
| 55 | Automotive dealers and gasoline service stations | 27.5 | 33.0 | 27.3 | 15.7 | 25.0 |
| 56 | Apparel and accessories | 19.4 | 14.4 | 11.6 | 7.8 | 13.0 |
| 57 | Furniture, home furnishings, and equipment | 16.9 | 12.4 | 9.1 | 6.5 | 10.7 |
| 58 | Eating and drinking places | 12.6 | 6.6 | 5.7 | 6.2 | 7.5 |
| 59 | Miscellaneous retail stores | 14.3 | 10.7 | 9.1 | 6.8 | 9.8 |
| | *Finance, insurance, and real estate* | | | | | |
| 60 | Banking | .9 | .7 | .8 | .8 | .8 |
| 61 | Credit agencies other than banks | 3.3 | 3.7 | 4.8 | 5.1 | 4.3 |
| 62 | Security and commodity brokers, dealers, exchanges, and services. | 2.8 | 1.5 | 1.5 | 2.4 | 2.1 |
| 63 | Insurance carriers | 2.4 | 2.4 | 2.8 | 3.2 | 2.7 |
| 64 | Insurance agents, brokers, and service | 8.3 | 9.5 | 10.0 | 10.3 | 9.6 |
| 65 | Real estate | 5.1 | 5.2 | 5.3 | 5.8 | 5.3 |
| 67 | Holding and other investment companies | 5.9 | 5.6 | 6.0 | 5.8 | 5.8 |
| | *Services* | | | | | |
| 70 | Hotels, rooming houses, camps, and other lodging places. | 9.6 | 8.6 | 8.1 | 7.8 | 8.5 |
| 72 | Personal services | 11.7 | 11.1 | 9.1 | 11.5 | 10.8 |
| 73 | Miscellaneous business services | 12.8 | 13.1 | 13.0 | 14.2 | 13.3 |
| 75 | Automobile repair services and garages | 14.8 | 13.7 | 12.5 | 10.6 | 12.7 |
| 76 | Miscellaneous repair services | 10.4 | 13.4 | 13.3 | 14.6 | 13.2 |
| 77 | Radio broadcasting, including facsimile broadcasting, and television. | 24.9 | 18.8 | 12.5 | 10.1 | 15.8 |
| 78 | Motion pictures | 19.4 | 14.6 | 9.2 | 8.4 | 12.7 |
| 79 | Amusement and recreation services except motion pictures. | 21.3 | 13.6 | 11.9 | 12.0 | 14.9 |
| 80, 81, 82, 84, 86, and 89 | Other services | 8.8 | 9.7 | 10.3 | 8.3 | 9.3 |

[1] Parentheses indicate negative rate of return.

§ 40.447–3 *Application required under section 447.* (a) The excess profits tax for any taxable year shall be determined by reference to section 442, 443, 444, 445, or 446 only if an application for the benefits of such section is filed by the taxpayer within the period specified in section 447 (e).

(b) The application shall be made by filing with the collector schedule EP–5 (Form 1120) together with the statement described below. If the application is made with the original return, it shall be filed with, and as a part of, Form 1120 for the taxable year. If the application is not filed with the original return, it shall be filed with, and as a part of, an amended return, or, if made in connection with a claim for credit or refund, it shall be filed with, and as a part of, the claim for credit or refund. If a petition is filed with the Tax Court for the redetermination of the tax under chapter 1 for the taxable year, the application shall be effective only if filed with the collector not later than the date on which the original petition is filed. The application, however filed, must include a statement setting forth in detail each ground upon which the taxpayer relies, and facts sufficient to apprise the Commissioner of the exact basis for the application. Section 442, 443, 444, 445, or 446 shall not be applied upon the basis of any ground other than those set forth in an application filed within the period prescribed in section 447 (e).

SEC. 448. EXCESS PROFITS CREDIT—REGULATED PUBLIC UTILITIES.

(a) *Amount of credit.* In the case of a regulated public utility (as defined in subsection (d)), the excess profits credit for any taxable year computed under this section shall be the sum of the tax imposed by sections 13, 14, 15, and 141 (c), for such taxable year and the amount determined under subsection (b).

(b) *Computation.* The amount referred to in subsection (a) for any taxable year shall be determined as follows:

(1) By applying to the sum of the following the per centum prescribed in subsection (c):

(A) The adjusted invested capital for such taxable year, and

(B) The average borrowed capital for such taxable year as defined in section 439.

For the purposes of this paragraph the adjusted invested capital for any taxable year shall be the amount computed for such year under section 437 (b) (2) without reduction by the amount of the net new capital addition and without regard to section 437 (b) (2) (C); except that in the case of a corporation described in subsection (c) (1) (A), (c) (1) (B), (c) (2), or (c) (4), the corporate books of account of which are maintained in accordance with systems of accounts prescribed by an appropriate regulatory body (or, if not so prescribed, are maintained in accordance with the uniform systems of accounts prescribed by the Federal Power Commission or the National Association of Railway and Utility Commissioners), the adjusted invested capital for such year shall be the sum of the average outstanding common and preferred capital stock accounts and the capital surplus and earned surplus accounts for such taxable year as recorded on such corporate books of account.

(2) By reducing the amount ascertained under paragraph (1) by the deduction allowable for such year with respect to interest on indebtedness included in borrowed capital under section 439.

(3) By reducing the amount ascertained under paragraph (2) by the amount computed under section 440 (b) (relating to inadmissible assets): except that in the case of a corporation described in subsection (c) (1) (A), (c) (1) (B), (c) (2), or (c) (4), the corporate books of account of which are maintained in accordance with systems of accounts prescribed by an appropriate regulatory body (or, if not so prescribed, are maintained in accordance with the uniform systems of accounts prescribed by the Federal Power Commission or the National Association of Railway and Utility Commissioners), in determining the amount computed under section 440, the amount attributable to each asset held at any time during such taxable year shall be determined according to such corporate books of account.

(c) The per centum referred to in subsection (b) (1) shall be:

(1) 6 per centum in the case of a corporation engaged in the furnishing or sale of—

(A) Electric energy, gas, water, or sewerage disposal services, or

(B) Transportation (not included in paragraph (3)) on an intrastate, suburban, municipal, or interurban electric railroad, on an intrastate, municipal, or suburban trackless trolley system, or on a municipal or suburban bus system, or

(C) Transportation (not included in subparagraph (B)) by motor vehicle—

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of the District of Columbia or of any State or political subdivision thereof.

(2) 6 per centum in the case of a corporation engaged as a common carrier in the furnishing or sale of transportation of gas by pipe line, if subject to the jurisdiction of the Federal Power Commission.

(3) 6 per centum in the case of a corporation engaged as a common carrier in the furnishing or sale of transportation by railroad, or in the furnishing or sale of transportation of oil or other petroleum products (including shale oil) by pipe line, subject to the jurisdiction of the Interstate Commerce Commission.

(4) 7 per centum in the case of a corporation engaged in the furnishing or sale of telephone or telegraph service, if the rates for such furnishing or sale meet the requirements of paragraph (1).

(5) 7 per centum in the case of a corporation engaged in the furnishing or sale of transportation as a common carrier by air, subject to the jurisdiction of the Civil Aeronautics Board.

(6) 6 per centum in the case of a corporation engaged in the furnishing or sale of transportation by common carrier by water, subject to the jurisdiction of the Interstate Commerce Commission under Part III of the Interstate Commerce Act, or subject to the jurisdiction of the Federal Maritime Board under the Intercoastal Shipping Act, 1933.

(d) For the purposes of this subchapter the term "regulated public utility" means (except as provided in subsection (e)) a corporation described in subsection (c), but only if 80 per centum or more of its gross income (computed without regard to dividends and capital gains and losses) for the taxable year is derived from sources described in subsection (c). If the taxpayer establishes to the satisfaction of the Secretary that—

(1) Its revenue from regulated rates described in subsection (c) (1) or (4) and its revenue derived from unregulated rates are derived from its operation of a single interconnected and coordinated system or from the operation of more than one such system, and

(2) The unregulated rates have been and are substantially as favorable to users and consumers as are the regulated rates,

such revenue from such unregulated rates shall be considered, for the purposes of this subsection, as income derived from sources described in subsection (c) (1) or (4).

(e) *Consolidated returns of regulated public utilities.* For provisions applicable to consolidated returns of regulated public utilities computing their excess profits credit under this section, see subsections (e) and (j) of section 141. For purposes of filing a consolidated return, a common parent corporation shall be deemed a regulated public utility if at least 80 per centum of its gross income (computed without regard to capital gains or losses) is derived directly or indirectly from sources described in subsection (c). For the purposes of the preceding sentence dividends or interest received from a regulated public utility shall be considered as derived from sources described in subsection (c) if the regulated public utility is a member of an affiliated group (as defined in section 141 (d)) which includes the common parent corporation.

§ 40.448–1 *Excess profits credit of regulated public utilities entitled to benefits of section 448.* Section 448 provides for certain regulated public utilities an excess profits credit which is an alternative to the excess profits credit based on income (section 435) and to the excess profits credit based on invested capital (section 436). This alternative excess profits credit shall be computed under §40.448–3.

§ 40.448–2 *Definitions*—(a) *Regulated public utility.* For the purpose of subchapter D of chapter 1, the term "regulated public utility" means (except as provided in section 448 (e) relating to consolidated returns of regulated public utilities) a corporation described in section 448 (c) and subparagraphs (1) through (6) of this paragraph, but only if 80 percent or more of its gross income, computed without regard to dividends and capital gains and losses, for the taxable year is derived from sources described in section 448 (c) and in subparagraphs (1) through (6), of this paragraph.

(1) A corporation engaged in the furnishing or sale of—

(i) Electric energy, gas, water, or sewerage disposal services, or

(ii) Transportation (not included in subparagraph (3) of this paragraph) on an intrastate, suburban, municipal, or interurban electric railroad, on an intrastate, municipal, or suburban trackless trolley system, or on a municipal or suburban bus system, or

(iii) Transportation (not included in subdivision (ii) of this subparagraph) by motor vehicle—

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of the District of Columbia or of any State or political subdivision thereof.

(2) A corporation engaged as a common carrier in the furnishing or sale of transportation of gas by pipeline, if subject to the jurisdiction of the Federal Power Commission.

(3) A corporation engaged as a common carrier in the furnishing or sale of transportation by railroad, or in the furnishing or sale of transportation of oil or other petroleum products (including shale oil) by pipeline, subject to the jurisdiction of the Interstate Commerce Commission.

(4) A corporation engaged in the furnishing or sale of telephone or telegraph service, if the rates for such furnishing or sale meet the requirements of subparagraph (1) of this paragraph.

(5) A corporation engaged in the furnishing or sale of transportation as a common carrier by air, subject to the jurisdiction of the Civil Aeronautics Board.

(6) A corporation engaged in the furnishing or sale of transportation by common carrier by water, subject to the jurisdiction of the Interstate Commerce Commission under Part III of the Interstate Commerce Act, or subject to the jurisdiction of the Federal Maritime Board under the Intercoastal Shipping Act, 1933.

If the taxpayer establishes to the satisfaction of the Commissioner that its revenue from regulated rates described in subparagraphs (1) or (4) of this paragraph, and from unregulated rates are derived from its operation of a single interconnected and coordinated system or from its operation of more than one such system, and that the unregulated rates have been and are substantially as favorable to users and consumers as the regulated rates, such revenue from such unregulated rates shall be considered, for the purpose of this paragraph, as income derived from sources described in subparagraphs (1) or (4) of this paragraph.

(b) *Normal tax and surtax.* The amount of the normal tax and surtax which is included in the excess profits credit computed under section 448 for any taxable year is the total amount of the tax imposed by sections 13, 14, 15, and 141 (c) for such taxable year. If an alternative tax is imposed by section 117 (c) for the taxable year, such alternative tax is included in lieu of the tax that otherwise would have been imposed for such year.

(c) *Adjusted invested capital.* For the purpose of computing the excess profits credit for any taxable year under section 448—

(1) In the case of a corporation which is a regulated public utility and is not described in subparagraph (2) of this paragraph, the adjusted invested capital for such year shall be the sum of (i) the equity capital (as defined in section 437 (c) and § 40.437–5) at the beginning of the taxable year, (ii) the average daily amount of money and property paid in for stock, or as paid-in surplus, or as a contribution to capital during the taxable year, and (iii) the recent loss adjustment (computed under section 437 (f) and § 40.437–8); reduced by the average daily amount of distributions made during the taxable year not out of the earnings and profits of such taxable year.

(2) In the case of a corporation described in paragraph (a) (1) (i) or (ii), (2) or (4) of this section, if the corporate books of account are maintained in accordance with systems of accounts prescribed by an appropriate regulatory body (or, if not so prescribed, are maintained in accordance with the uniform systems of accounts prescribed by the Federal Power Commission or the National Association of Railway and Utility Commissioners), the adjusted invested capital for such year shall be the sum of the average outstanding common and preferred capital stock accounts for the taxable year and the capital surplus and earned surplus accounts at the beginning of the taxable year as properly recorded on the corporate books of account. In order to establish its right to compute its adjusted invested capital by this method for any taxable year, the taxpayer must attach a statement to its return for such taxable year setting

forth all the facts relied on as qualifying the taxpayer to use such method.

(d) *Inadmissible assets.* For the purpose of section 448, the term "inadmissible assets" means inadmissible assets as defined in section 440 (a). In computing the ratio of inadmissible assets to total assets the amount attributable to each asset shall be determined as provided in section 440 (b), except that in the case of a corporation described in paragraph (a) (1) (i) or (ii), (2), or (4), of this section, if the corporate books of account are maintained in accordance with systems of accounts prescribed by an appropriate regulatory body (or, if not so prescribed, are maintained in accordance with the uniform systems of accounts prescribed by the Federal Power Commission or National Association of Railway and Utility Commissioners), the amount attributable under section 440 (b) to each asset shall be determined according to the amounts properly recorded in the corporate books of account.

§ 40.448–3 *Computation of excess profits credit.* The excess profits credit of a regulated public utility is determined under section 448 as follows:

(a) The sum of the adjusted invested capital (§ 40.448–2 (c)) and the average daily amount of borrowed capital of the taxpayer for the taxable year is multiplied by 6 percent in the case of a corporation described in § 40.448–2 (a) (1), (2), (3), or (6), or by 7 percent in the case of a corporation described in § 40.448–2 (a) (4) or (5).

(b) The amount ascertained under paragraph (a) of this section is reduced by the amount of the deduction allowable for the taxable year with respect to interest on the indebtedness included in (a) as borrowed capital.

(c) The amount ascertained under paragraph (b) of this section is reduced by the amount computed under section 440 (b), relating to inadmissible assets. See § 40.448–2 (d).

(d) The amount ascertained under paragraph (c) of this section is added to the amount of the corporation's normal tax and surtax for the taxable year. See § 40.448–2 (b).

SEC. 449. PERSONAL SERVICE CORPORATIONS.

(a) *Definition.* As used in this subchapter, the term "personal service corporation" means a corporation whose income is to be ascribed primarily to the activities of shareholders who are regularly engaged in the active conduct of the affairs of the corporation and are the owners at all times during the taxable year of at least 70 per centum in value of each class of stock of the corporation, and in which capital is not a material income-producing factor; but does not include any foreign corporation, nor any corporation 50 per centum or more of whose gross income consists of gains, profits, or income derived from trading as a principal. For the purposes of this subsection, an individual shall be considered as owning, at any time, the stock owned at such time by his spouse or minor child or by any guardian or trustee representing them.

(b) *Election as to taxability.* If a personal service corporation signifies, in its return under this chapter for any taxable year, its desire not to be subject to the tax imposed under this subchapter for such taxable year, it shall be exempt from such tax for such year, and the provisions of Supplement S of this chapter shall apply to the shareholders in such corporation who were such shareholders on the last day of such taxable year of the corporation. Such corporation shall not be exempt for such year if it is a member of an affiliated group of corporations filing consolidated returns under section 141.

§ 40.449–1 *Taxation of personal service corporations.* A personal service corporation is subject to the excess profits tax imposed under subchapter D of chapter 1 the same as any other domestic corporation unless it elects as to any taxable year not to be subject to such tax. Such an election may not be exercised by a corporation filing a consolidated return under section 141. If a corporation is exempt by reason of the exercise of such an election, the provisions of Supplement S of chapter 1 (sections 391 to 396, inclusive) shall apply to the shareholders in such corporation who were such shareholders on the last day of the taxable year of the corporation. See § 29.394–1 of Regulations 111. In such case, the amount of the undistributed Supplement S net income shall be considered as paid in to the corporation as of the close of the taxable year as paid-in surplus or as a contribution to capital, and the amount of accumulated earnings and profits as of the close of such year shall be correspondingly reduced. See section 394 (d).

§ 40.449–2 *Definition of personal service corporations*—(a) *In general.* The term "personal service corporation" means a domestic corporation in which capital is not a material income-producing factor and the income of which is to be ascribed primarily to the activities of shareholders who (1) are regularly engaged in the active conduct of the affairs of the corporation, and (2) are the owners, throughout the entire taxable year of at least 70 percent in value of each class of stock of the corporation. If 50 percent or more of the gross income of a corporation consists of gains, profits, or income derived from trading as a principal, such corporation cannot be considered to be a personal service corporation. As to corporations in which less than 50 percent of the gross income is derived from trading as a principal, see paragraph (c) of this section.

(b) *Stock interest of shareholders.* (1) Shareholders regularly engaged in the active conduct of the affairs of the corporation and to whom the income of the corporation is primarily to be ascribed must own at all times during the taxable year at least 70 percent in value of each class of stock of the corporation. If stock is owned by the spouse or minor child of an individual, or owned by the guardian or trustee of such spouse or child, such stock is treated as being owned by such individual.

(2) A corporation cannot be considered to be a personal service corporation for any taxable year if another corporation owns more than 30 percent in value of any class of its stock at any time during such year. A corporation is an artificial entity and cannot itself be regularly engaged in the active conduct of the affairs of another corporation within the meaning of section 449.

(3) The fact that the ownership of shares in the corporation may change during the course of the taxable year does not take the corporation which is otherwise a personal service corporation out of that class unless at some time during the taxable year the ownership of more than 30 percent in value of the shares of any class of stock passes into the hands of persons not regularly engaged in the active conduct of the affairs of the corporation.

(c) *Income to be ascribed primarily to the activities of shareholders.* (1) If employees other than shareholders contribute substantially to the services rendered by a corporation, such corporation is not a personal service corporation unless, in every case in which services are so rendered, the value of and the compensation charged for such services are to be attributed primarily to the experience or skill of the shareholders and such fact is evidenced in some definite manner in the normal course of the business or profession. The fact that the shareholders give personal attention or render valuable services to the corporation as a result of which its earnings are greater than those of a corporation engaged in a like or similar business or profession, the shareholders of which are not regularly engaged in the activities of the corporation, does not of itself constitute the corporation a personal service corporation.

(2) Income of a corporation from merchandising or trading as a principal, directly or indirectly, in commodities or in the services of others is not to be ascribed primarily to the activities of its shareholders. Income of a corporation from the conduct of an auction, agency, brokerage, or commission business strictly on the basis of a fee or commission may be so ascribed. If, however, either as a matter of business policy or by contract, the corporation assumes any such risks as those of market fluctuations, bad debts, or failure to accept shipments, or if it guarantees the accounts of the purchaser or is in any way accountable to the seller for the payment of the purchase price, the transaction is one of merchandising or trading, and this is true even though the goods are shipped directly from the producer to the consumer and are never actually in the possession of the corporation. The fact that earnings of the corporation are termed commissions or fees is not controlling. The fact that a commission or fee in a transaction is based on a difference in the prices at which the seller sells and the buyer buys raises a presumption that the transaction is one of merchandising or trading, and it will be so considered in the absence of satisfactory evidence to the contrary.

(3) It may happen that a corporation is engaged in two or more businesses or professions which are more or less related. Thus, an engineering concern may also engage in contracting, which amounts to trading in materials and labor, or a brokerage concern may guarantee some of its accounts, or a photographic concern may sell pictures, frames, art goods, and supplies. In such cases, the corporation is not a personal service corporation unless the activities of the corporation consisting of trading or guaranteeing of accounts or selling

are negligible or merely incidental, and unless no appreciable part of the earnings is to be ascribed to such activities. See also paragraph (e) of this section, relating to the employment of capital.

(d) *Shareholders regularly engaged in the active conduct of the affairs of the corporation.* A corporation is not a personal service corporation unless shareholders who own at all times during the taxable year at least 70 percent in value of each class of stock are regularly engaged in the active conduct of the affairs of the corporation. That such shareholders devote some of their time to the affairs of the corporation is not sufficient; they must with regularity devote substantial time and energy to the conduct of its affairs.

(e) *Capital as a material income-producing factor.* (1) In a personal service corporation capital must not be a material income-producing factor. Whether capital is a material income-producing factor is to be determined by reference to (i) the extent to which capital is required to carry on the business or profession and (ii) the extent to which capital is actually used in the production of income though not required by the primary activities of the corporation. If the use of capital is necessary to the production of the income of the corporation and is more than incidental, capital is a material income-producing factor and the corporation is not a personal service corporation. If a substantial portion of the income is attributable to a use of capital, whether or not connected with the primary activities of the corporation, capital is a material income-producing factor even though such use of capital is not necessary to such primary activities. The term "capital" as used in section 449 and in this section means not only capital actually invested by the shareholders but also capital obtained in other ways. Thus, capital may be borrowed either directly as shown by bonds, debentures, certificates of indebtedness, notes, bills payable, or other paper, or indirectly as shown by accounts payable or other forms of credit, or the business of the corporation may be financed in some other manner by its shareholders. If a substantial amount of capital is used to finance or carry the accounts of clients or customers, it will be inferred that because of competition or for other reasons such use of capital is necessary and more than incidental in order to secure or hold business which would otherwise be lost. If a corporation engaged in an agency, brokerage, or commission business regularly employs a substantial amount of capital to lend to its principals, to buy and carry goods on its own account, or to buy and carry odd lots in order that it may render more satisfactory service to its principals or customers, such corporation is not a personal service corporation. In general, the larger the amount of capital actually used the stronger is the evidence that capital is necessary and more than incidental and is a material income-producing factor.

(2) The term "income" as used in section 449 and in this section means gross income. Capital is a material income-producing factor if its use results in a substantial amount of gross income, irrespective of the amount of net income, if any, such use produces.

(f) *Application of regulations; returns.* No definite and conclusive tests can be prescribed by which it can be finally determined in advance of an examination of the corporation's income tax return whether it is or is not a personal service corporation. In the preceding subsections are set forth the general principles under which such determination will be made. If a corporation claiming to be a personal service corporation signifies in its return for any taxable year its desire not to be subject to the excess profits tax, it shall attach and file Schedule PS (Form 1120) with, and as a part of, its return on Form 1120. In Schedule PS (Form 1120) there shall be stated (1) such facts as tend to show whether or not the corporation is a personal service corporation, including (i) the nature of its business, (ii) the character, preferences, dividend rates, and other essential features of the various classes of its stock outstanding for any time during the taxable year, (iii) the names and addresses of its several shareholders and their relationship to each other, (iv) the number and classes of shares owned at any time during the taxable year by each shareholder and the portion of the year during which such shares were so owned, (v) the nature of the activities of the several shareholders on behalf of the corporation, and (vi) the extent to which capital in any form is used in the business, and (2) the computation of the undistributed Supplement S net income for the taxable year, the names and addresses of all shareholders of the corporation at the close of the taxable year, the number and classes of shares held by each, and such other information as may be required by the form and the instructions printed on the form or issued therewith.

§ 40.449–3 *Election as to taxability.* The election as to taxability provided for in section 449 (b) and the exemption from tax, where such is allowable, have application only to the excess profits tax on domestic corporations imposed under subchapter D of chapter 1. The corporation may make such an election by signifying in its return its desire not to be subject to the excess profits tax. A new election is required for each taxable year. An amended return filed after the statutory period for filing the return (or after the last day of any extension period) is not a return within the meaning of section 449 (b).

SEC. 450. CORPORATIONS ENGAGED IN MINING OF STRATEGIC MINERALS.

(a) *Exemption from tax.* In the case of any domestic corporation engaged in the mining of a strategic mineral, the portion of the adjusted excess profits net income attributable to such mining in the United States shall be exempt from the tax imposed by this subchapter. The tax on the remaining portion of such adjusted excess profits net income shall be an amount which bears the same ratio to the tax computed without regard to this section as such remaining portion bears to the entire adjusted excess profits net income.

(b) *Definitions.* For the purposes of this section—

(1) The term "strategic mineral" means antimony, chromite, manganese, nickel, platinum (including the platinum group metals), quicksilver, sheet mica, tantalum, tin, tungsten, vanadium, fluorspar, flake graphite, vermiculite, perlite, long-fibre asbestos in the form of amosite, chrysotile or crocidolite, beryl, cobalt, columbite, corundum, diamonds, kyanite (if equivalent in grade to Indian kyanite), molybdenum, monazite, quartz crystals, and uranium, and any other mineral which the certifying agency has certified to the Secretary as being essential to the defense effort of the United States and as not having been normally produced in appreciable quantities within the United States.

(2) The term "certifying agency" means the department, official, corporation, or agency utilized or created to carry out the authority of the President under section 303 (a) of the Defense Production Act of 1950 to make provision for the encouragement of exploration, development, and mining of critical and strategic minerals and metals.

(c) *Certification during taxable year of taxpayer.* In determining under subsection (a) the portion of the adjusted excess profits net income which is attributable to the mining of a mineral which is a strategic mineral by reason of a certification made during the taxable year, such portion shall be an amount which bears the same ratio to the portion of the adjusted excess profits net income, determined without regard to this subsection, attributable to such mining during the entire taxable year as the number of days for which the taxpayer held the mineral property during the taxable year and after the date of the making of the certification bears to the number of days for which the taxpayer held the property during such taxable year.

(d) *Application of section to lessor.* In the case of a mining property operated under a lease, income attributable to such property derived by a lessor corporation shall, for the purposes of this section, be considered to be income of a corporation engaged in mining.

§ 40.450–1 *Corporations which mine strategic minerals.* (a) If a domestic corporation is engaged in mining a strategic mineral (as defined in section 450 (b)) within the United States, the portion of its adjusted excess profits net income attributable to such mining is exempt from excess profits tax. The excess profits tax on the remaining portion of such adjusted excess profits net income is an amount which bears the same ratio to the excess profits tax computed without regard to section 450 as such remaining portion bears to the entire adjusted excess profits net income.

(b) The portion of the adjusted excess profits net income attributable to mining of strategic minerals is an amount which bears the same ratio to the total adjusted excess profits net income as the portion of the excess profits net income attributable to such mining bears to the total excess profits net income. For any taxable year, the portion of the excess profits net income attributable to such mining is the gross income derived from strategic minerals and arising out of operations which give rise to "gross income from the property," as defined in § 29.23 (m)–1 (*j*) of Regulations 111, less the sum of (1) allowable deductions which are directly attributable to such mining for such year, (2) any adjustments made under the provisions of section 433 applicable to such year involving items directly attribut-

able to such mining, and (3) an allocable portion of any deductions partly attributable to such mining and of any adjustments under the provisions of section 433 applicable to such year involving items partly attributable to such mining.

(c) If a mineral is certified to the Secretary during the taxable year to be a strategic mineral, the portion of the adjusted excess profits net income which is attributable to the mining of such mineral shall be an amount which bears the same ratio to the portion of the adjusted excess profits net income, determined under paragraph (b) of this section without regard to this sentence, attributable to such mining during the entire taxable year as the number of days which the taxpayer held the property during the taxable year and after the date of the making of the certification bears to the total number of days for which the taxpayer held the property during such taxable year.

(d) There shall be attached to and made a part of the return of any taxpayer claiming the benefits under section 450 a schedule containing the following information:

(1) The amount of gross income from the mining of strategic minerals and from each other activity of the corporation;

(2) The allowable deductions and the adjustments under section 433 directly attributable to such mining; and

(3) The portion of the allowable deductions and of the adjustments under section 433 allocated to such mining and the basis for such allocation.

(e) In the case of a mining property operated under a lease, income attributable to such property derived by a lessor corporation, which is a domestic corporation, shall for the purposes of section 450, be considered to be income of a corporation engaged in mining.

SEC. 451. CAPITALIZATION OF ADVERTISING, ETC., EXPENDITURES.

(a) *Election to charge to capital account.* For the purpose of computing the excess profits credit, a taxpayer may elect, within six months after the date prescribed by law for filing its return for its first taxable year under this subchapter, to charge to capital account so much of the deductions for taxable years in its applicable base period on account of expenditures for advertising or the promotion of good will, as, under rules and regulations prescribed by the Secretary, may be regarded as capital investments. Such election must be the same for all such taxable years, and must be for the total amount of such expenditures which may be so regarded as capital investments. In computing the excess profits credit, no amount on account of such expenditures shall be charged to capital account:

(1) For taxable years in the base period unless the election authorized in this subsection is exercised, or

(2) For any taxable year prior to the beginning of the base period.

The election provided by this subsection shall be available with respect to expenditures to establish, maintain or increase the circulation of a newspaper, magazine or other periodical notwithstanding the provisions of section 204 (b) of the Revenue Act of 1950.

(b) *Effect of Election.* If the taxpayer exercises the election authorized under subsection (a)—

(1) The net income for each taxable year in the base period shall be considered to be the net income computed with such deductions disallowed, and such deductions shall not be considered as having diminished earnings and profits. This paragraph shall be retroactively applied as if it were a part of the law applicable to each taxable year in the base period; and

(2) The treatment of such expenditures as deductions for a taxable year in the base period shall, for the purposes of section 452 (b) be considered treatment which was not correct under the law applicable to such year.

§ 40.451–1 *Scope of election to charge to capital account expenditures for advertising or the promotion of good will.* (a) Any taxpayer may, for the purpose of computing its excess profits credit under either the income or the invested capital method, elect to charge to capital account any deductions based upon expenditures for taxable years in its base period on account of advertising or the promotion of good will, to the extent that such expenditures may be regarded as capital investments under the regulations prescribed under section 451. Section 451 provides for an election with reference only to deductions for such expenditures for taxable years in the base period. In order to secure the benefits of that section an election must be made by the taxpayer within six months after the date prescribed by law for filing its return for its first taxable year ending after June 30, 1950.

(b) The election under section 451 is an election to capitalize all the expenditures in each taxable year in the taxpayer's base period which were for advertising or the promotion of good will and which may be regarded as capital investments under the regulations prescribed under section 451. A taxpayer may not capitalize such expenditures for one base period taxable year and treat as a deduction such expenditures with respect to another base period taxable year. No such expenditures for any taxable year prior to the beginning of taxpayer's base period may be charged to capital account. A taxpayer which has failed to make an election under section 451 is not permitted, in computing its excess profits credit, to charge to capital account base period expenditures for advertising or the promotion of good will which have been deducted for taxable years in such period. The election provided by section 451 (a) and by this section shall be available with respect to those expenditures to establish, maintain, or increase the circulation of a newspaper, magazine, or other periodical, which may be regarded as capital expenditures under the regulations prescribed under section 451, not withstanding the provisions of section 23 (bb).

§ 40.451–2 *Expenditures which may be regarded as capital investments.* (a) An expenditure for advertising or the promotion of good will, including an expenditure to establish, maintain, or increase the circulation of a newspaper, magazine, or other periodical, may be regarded as a capital investment if, upon consideration of all the facts and circumstances of the particular case, it may be regarded as made for the purpose of increasing the taxpaper's earning capacity over a substantial period subsequent to the taxable year in which such expenditure was made. The fact that a corporation failed, because of operating losses, to receive any benefits with respect to its income tax liability from deductions on account of expenditures is not evidence that such expenditures may be regarded as capital investments. In addition to those expenditures for capital items including good will which, under the provisions of section 24, may not be allowed as deductions, the following expenditures may in any case be regarded as capital investments within the contemplation of section 451:

(1) All advertising expenditures to promote a taxpayer's business in a territory new to such taxpayer, or to promote a new product, department, trade-mark, trade brand, or trade name of such taxpayer, for the first 12 months after the taxpayer has begun to develop such new territory or to promote such new product, department, trade-mark, trade brand, or trade name. A new product within the meaning of this section does not include any product which is merely an improvement of an earlier product.

(2) All advertising expenditures for the taxable year to the extent that such expenditures exceed the taxpayer's average annual expenditures on account of advertising for the 48 months preceding the taxable year, or, if the taxpayer was not in existence during the whole of such 48-month period, then for the period during which the taxpayer was in existence.

(3) In the case of expenditures to establish, maintain, or increase the circulation of a newspaper, magazine, or periodical, the portion of such expenditures which, pursuant to regulations prescribed under section 23 (bb), would be chargeable to capital account if the taxpayer made the election provided in section 23 (bb).

(b) Every item classifiable under this section as a capital investment constitutes a permanent asset of the taxpayer's business, and no deduction for depreciation will be allowed in respect of such an item.

(c) A taxpayer which has made the election under section 451 may not deduct for any excess profits tax taxable year expenditures made in such year similar to expenditures made during its base period for advertising or the promotion of good will which are treated under section 451 for the purposes of its excess profits credit as capital investments. Such a taxpayer has the burden of proving that expenditures for advertising or the promotion of good will which it seeks to deduct for such excess profits tax taxable year may not be regarded as capital investments under the provisions of this section. The taxpayer shall submit with its excess profits tax return a statement containing complete information with respect to all expenditures for advertising or the promotion of good will made during its excess profits tax taxable year, classified as to those which are deductible and those which may be regarded as capital investments under section 451. The statement filed with the return shall also set forth

whether such expenditures were extraordinary in nature or amount and the purpose for which they were made.

§ 40.451-3 *Effect of election.* (a) Section 451 retroactively amends, for the purpose of determining the income tax liability and the excess profits credit of any taxpayer exercising an election under that section, the revenue laws applicable to each of such taxpayer's base period taxable years. Hence, the previous treatment as deductions of expenditures made during the base period which may be regarded as capital investments under the regulations prescribed under section 451 is an erroneous and inconsistent treatment. The normal-tax net income for each applicable base period taxable year must be recomputed with such expenditures disallowed as deductions, and both the excess profits net income for each such year and the earnings and profits account will be increased in the amount of such disallowed deductions.

(b) The disallowance of deductions in the base period made necessary by this section requires a redetermination of the income tax liability for such years and any deficiencies in tax resulting from the disallowance of such deductions shall be assessed and collected under the internal revenue laws applicable with respect to the assessment and collection of deficiencies for such years. If, however, correction of the effect of the prior inconsistent treatment of such items in the base period years is prevented, within the meaning of section 452 (b) (1) (C), correction shall be made by means of an adjustment under section 452. Since the amount of such an adjustment under section 452 is a part of the excess profits tax, which applies only to taxable years ending after June 30, 1950, it does not decrease earnings and profits or excess profits net income for any period before the beginning of the taxpayer's first excess profits tax taxable year.

(c) In the case of a taxpayer electing under section 451, the provisions of section 433 (b) (9), relating to abnormal deductions in the base period, do not affect deductions for expenditures for advertising or the promotion of good will which may be regarded as capital investments, since, in such a case, section 451 effects a disallowance of such deductions for income tax purposes before any of the adjustments under section 433 (b) are operative.

SEC. 452. ADJUSTMENT IN CASE OF POSITION INCONSISTENT WITH PRIOR INCOME TAX LIABILITY.

(a) *Definitions.* For the purposes of this section:

(1) *Taxpayer.* The term "taxpayer" means any person subject to a tax under the applicable revenue act.

(2) *Income tax.* The term "income tax" means an income tax imposed by this chapter or subchapter A of chapter 2 of this title; Title I and Title IA of the Revenue Acts of 1938, 1936, and 1934; Title I of the Revenue Acts of 1932 and 1928; Title II of the Revenue Acts of 1926 and 1924; Title II of the Revenue Acts of 1921 and 1918; Title I of the Revenue Act of 1917; Title I of the Revenue Act of 1916; or section II of the Act of October 3, 1913; a war profits or excess profits tax imposed by chapter 2E of this title; Title III of the Revenue Acts of 1921 and 1918; or Title II of the Revenue Act of 1917; or an income, war profits, or excess profits tax imposed by any of the foregoing provisions, as amended or supplemented.

(3) *Prior taxable year.* A taxable year ending after June 30, 1950, shall not be considered a prior taxable year.

(4) The term "predecessor of the taxpayer" means—

(A) A person which is a component corporation of the taxpayer within the meaning of Part II; and

(B) A person which on July 1, 1950, or at any time thereafter, controlled the taxpayer. The term "controlled" as herein used shall have the same meaning as "control" under section 112 (h); and

(C) Any person in an unbroken series ending with the taxpayer if subparagraph (A) or (B) would apply to the relationship between the parties.

(b) *Circumstances of adjustment:*

(1) If

(A) In determining at any time the tax of a taxpayer under this subchapter an item affecting the determination of the excess profits credit is treated in a manner inconsistent with the treatment accorded such item in the determination of the income tax liability of such taxpayer or a predecessor for a prior taxable year or years, and

(B) The treatment of such item in the prior taxable year or years consistently with the determination under this subchapter would effect an increase or decrease in the amount of the income taxes previously determined for such taxable year or years, and

(C) On the date of such determination of the tax under this subchapter correction of the effect of the inconsistent treatment in any one or more of the prior taxable years is prevented (except for the provisions of section 3801) by the operation of any law or rule of law (other than section 3761, relating to compromises),

then the correction shall be made by an adjustment under this section. If in a subsequent determination of the tax under this subchapter for such taxable year such inconsistent treatment is not adopted, then the correction shall not be made in connection with such subsequent determination.

(2) Such adjustment shall be made only if there is adopted in the determination a position maintained by the Secretary (in case the net effect of the adjustment would be a decrease in the income taxes previously determined for such year or years) or by the taxpayer with respect to whom the determination is made (in case the net effect of the adjustment would be an increase in the income taxes previously determined for such year or years) which position is inconsistent with the treatment accorded such item in the prior taxable year or years which was not correct under the law applicable to such year.

(3) *Burden of proof.* In any proceeding before the Tax Court or any other court the burden of proof in establishing that an inconsistent position has been taken (A) shall be upon the Secretary, in case the net effect of the adjustment would be an increase in the income taxes previously determined for the prior taxable year or years, or (B) shall be upon the taxpayer, in case the net effect of the adjustment would be a decrease in the income taxes previously determined for the prior taxable year or years.

(c) *Method and effect of adjustment.* (1) The adjustment authorized by subsection (b), in the amount ascertained as provided in subsection (d), if a net increase, shall be added to, and, if a net decrease, shall be subtracted from, the tax otherwise computed under this subchapter for the taxable year with respect to which such inconsistent position is adopted.

(2) If more than one adjustment under this section is made because more than one inconsistent position is adopted with respect to one taxable year under this subchapter, the separate adjustments, each an amount ascertained as provided in subsection (d), shall be aggregated, and the aggregate net increase or decrease shall be added to or subtracted from the tax otherwise computed under this subchapter for the taxable year with respect to which such inconsistent positions are adopted.

(3) If all the adjustments under this section, made on account of the adoption of an inconsistent position or positions with respect to one taxable year under this subchapter, result in an aggregate net increase, the tax imposed by this subchapter shall in no case be less than the amount of such aggregate net increase.

(4) If all the adjustments under this section, made on account of the adoption of an inconsistent position or positions with respect to a taxable year under this subchapter (hereinafter in this paragraph called the current taxable year), result in an aggregate net decrease, and the amount of such decrease exceeds the tax imposed by this subchapter (without regard to the provisions of this section) for the current taxable year, such excess shall be subtracted from the tax imposed by this subchapter for each succeeding taxable year, but the amount of the excess to be so subtracted shall be reduced by the reduction in tax for intervening taxable years which has resulted from the subtraction of such excess from the tax imposed for each such year.

(d) *Ascertainment of amount of adjustment.* In computing the amount of an adjustment under this section there shall first be ascertained the amount of the income taxes previously determined for each of the prior taxable years for which correction is prevented. The amount of each such tax previously determined for each such taxable year shall be (1) the tax shown by the taxpayer, or by the predecessor, upon the return for such prior taxable year, increased by the amounts previously assessed (or collected without assessment) as deficiencies and decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax; or (2) if no amount was shown as the tax by such taxpayer or such predecessor upon the return, or if no return was made by such taxpayer or such predecessor, then the amounts previously assessed (or collected without assessment) as deficiencies, but such amounts previously assessed, or collected without assessment, shall be decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax. There shall then be ascertained the increase or decrease in each such tax previously determined for each such year which results solely from the treatment of the item consistently with the treatment accorded such item in the determination of the tax liability under this subchapter. To the increase or decrease so ascertained for each such tax for each such year there shall be added interest thereon computed as if the increase or decrease constituted a deficiency or an overpayment, as the case may be, for such prior taxable year. Such interest shall be computed to the fifteenth day of the third month following the close of the excess profits tax taxable year with respect to which the determination is made. There shall be ascertained the difference between the aggregate of such increases, plus the interest attributable to each, and the aggregate of such decreases, plus the interest attributable to each, and the net increase or decrease so ascertained shall be the amount of the adjustment under this section with respect to the inconsistent treatment of such item.

(e) *Interest in case of net increase or decrease.* (1) If an adjustment under this section results in a net decrease, or more than one adjustment results in an aggregate net decrease, the portion of such net decrease or aggregate net decrease, as the case may be, subtracted from the tax which represents interest shall be included in gross income

of the taxable year in which falls the date prescribed for the payment of the tax under this subchapter.

(2) If an adjustment under this section results in a net increase, or more than one adjustment results in an aggregate net increase, the portion of such net increase or aggregate net increase, as the case may be, which represents interest shall be allowed as a deduction in computing net income for the taxable year in which falls the date prescribed for the payment of the tax under this subchapter.

§ 40.452–1 *Purpose and scope of section 452*—(a) *General.* Section 452 provides for an adjustment if a determination of a taxpayer's excess profits tax liability treats an item or transaction affecting the excess profits credit inconsistently with the treatment of such item or transaction in the determination of the income tax liability of the taxpayer, or a predecessor, for a prior taxable year or years. The adjustment is not authorized unless (1) the treatment of the item or transaction for prior taxable years was incorrect under the law applicable to such years, (2) a correction of the effect of such erroneous treatment for one or more of the prior taxable years is prevented by the operation of a provision or rule of law, and (3) the inconsistent position adopted in the determination is asserted and maintained by the party (either the Commissioner or the taxpayer) who would be adversely affected by the adjustment.

(b) *Definitions.* When used in §§ 40.452–1 to 40.452–4, inclusive

(1) The terms "taxpayer," "income tax," and "prior taxable year," shall have the meaning assigned to such terms by section 452 (a). As to what constitutes a taxable year, see section 48 (a).

(2) (i) The term "predecessor of the taxpayer" shall have the meaning assigned to such term by section 452 (a) (4) It is specifically provided that the term "controlled" as used in such definition shall have the same meaning as "control" under the definition contained in section 112 (h). Accordingly, a person is a predecessor of the taxpayer if, on July 1, 1950, or at any time thereafter, such person owned stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of the taxpayer. For the purpose of section 452 it is immaterial that such control did not exist during the taxable year in respect of which the incorrect treatment of the item or transaction occurred, or during the taxable year in respect of which the inconsistent position is adopted in the determination of the excess profits credit of the taxpayer.

(ii) Any person which is a component corporation of the taxpayer under the definition contained in section 461 is a predecessor of the taxpayer within the meaning of section 452. Such person may be a corporation, partnership, or a sole proprietor. Any such component corporation is a predecessor of the taxpayer irrespective of the method employed in computing the excess profits credit of the taxpayer.

(iii) Under the terms of the definition, any person which is a predecessor of a predecessor in an unbroken series ending with the taxpayer is a predecessor of the taxpayer within the meaning of section 452.

(iv) The limitation of the term "predecessor of the taxpayer" to certain cases, and the resulting exclusion of other cases, should not be construed to affect the established judicial doctrines commonly known as estoppel, recoupment, set-off, etc., which may be applied by the courts in appropriate cases.

§ 40.452–2 *Circumstances of adjustment*—(a) *Determination.* A final determination of the excess profits tax liability is not a prerequisite to an adjustment under section 452. Whenever there is a determination of the excess profits tax liability and the conditions prescribed in section 452 (b) are satisfied, the adjustment is authorized as an essential part of the determination of such tax liability. For example, the making of a return for excess profits tax purposes is a determination by the taxpayer; the assertion of a deficiency or the allowance or disallowance of a claim for refund is a determination by the Commissioner; and a decision by The Tax Court of the United States or a court is a determination by such Tax Court or court. If any such determination becomes final, the adjustment also becomes final. If, following a determination, there are further proceedings in the case and a subsequent determination which does not adopt the inconsistent treatment of the item or transaction, then no adjustment is authorized as a part of such subsequent determination.

(b) *Correction under ordinary procedure prevented.* (1) An adjustment is authorized only if, on the date of the determination of the excess profits tax liability, correction of the effect of the inconsistent treatment for one or more of the prior taxable years is prevented (except for the provisions of section 3801, relating to mitigation of effect of limitations and other provisions in income tax cases) by the operation, whether before, on, or after the date of enactment of section 452, of any provision of law (other than section 3761, relating to compromises) or rule of law. Such provisions or rules of law include, for example, statutes of limitations and res judicata.

(2) The ascertainment of whether correction of the effect of the inconsistent treatment is prevented within the meaning of section 452 (b) (1) (C) and this section must be made with respect to each income tax for each prior taxable year affected by the erroneous treatment of the item or transaction. Section 452 is not applicable in respect of any income tax for any prior taxable year if, on the date of the determination of the excess profits tax liability, correction of the effect of the erroneous treatment of the item is possible under the ordinary procedure applicable to the assessment and collection of deficiencies or the refund or credit of overpayments, as the case may be, in respect of such tax for such taxable year. See the example under § 40.452–4.

(3) If correction of the effect of the erroneous treatment of the item or transaction with respect to an income tax for a prior taxable year is otherwise prevented, the application of section 452 is not precluded by the fact that the tax for such year may, under appropriate circumstances, be open to an adjustment under section 3801.

(4) If any income tax liability for a prior taxable year has been compromised under section 3761, no adjustment may be made under section 452 with respect to the tax liability compromised.

(c) *Operation dependent upon maintenance of inconsistent position.* (1) An adjustment, with respect to an item or transaction, which would result in a net increase in the amount of the income taxes previously determined for prior taxable years is authorized only if (i) the taxpayer with respect to which the determination is made has, in connection with an item or transaction affecting the determination of its excess profits credit, maintained a position which is inconsistent with the erroneous treatment of such item or transaction for prior taxable years, and (ii) such inconsistent position is adopted in the determination.

(2) An adjustment, with respect to an item or transaction, which would result in a net decrease in the amount of the income taxes previously determined for prior taxable years is authorized only if (i) the Commissioner, in connection with an item or transaction affecting the determination of the taxpayer's excess profits credit, has maintained a position which is inconsistent with the erroneous treatment of such item or transaction for prior taxable years, and (ii) such inconsistent position is adopted in the determination.

(3) Neither the Commissioner nor the taxpayer is required to adopt an inconsistent position with respect to the treatment of an item or transaction in the determination of the excess profits credit because of the fact that such item or transaction was incorrectly treated in the determination of the income tax liability of the taxpayer, or a predecessor, for a prior taxable year or years, under the law applicable to such year or years. Such item or transaction may, in the determination of the excess profits credit, be treated in a manner consistent with the incorrect treatment accorded in the determination of the income tax liability if neither the Commissioner nor the taxpayer objects. Either the Commissioner or the taxpayer, however, may insist upon the correct treatment of such item or transaction in the determination of the excess profits credit under the law applicable to the excess profits tax taxable year, but such action constitutes the maintenance of an inconsistent position and will result in an adjustment under section 452, if the party insisting upon such treatment is the party who would be adversely affected by such adjustment.

(4) A taxpayer which has taken an inconsistent position with respect to an item or transaction affecting the determination of its excess profits credit may, upon notice to the Commissioner in writing, withdraw from such position.

(5) Inconsistent treatment within the meaning of section 452 may relate to the

principle or rule of law applied in determining the taxable status of an item or transaction, or it may relate only to the amount of the item or transaction which is to be taken into account for tax purposes. The inconsistency is to be ascertained by reference to the actual treatment of the item or transaction for prior taxable years rather than to what the taxpayer or the Commissioner may have urged.

(6) If a determination of the excess profits tax liability for one taxable year adopts with respect to an item or transaction an inconsistent position which results in an adjustment under section 452, similar treatment of the same item or transaction for subsequent excess profits tax taxable years does not authorize a further adjustment under such section.

(d) *Law applicable in determination of error.* (1) Whether there was an erroneous treatment of the item or transaction for prior taxable years is to be determined under the provisions of the internal revenue laws applicable with respect to such years. If the inconsistent treatment adopted in the determination of the excess profits tax liability is based upon an authoritative judicial interpretation of the applicable revenue law which differs from the interpretation of such law accepted in the determination of the tax liability for such prior years, then the treatment accorded the item or transaction for such prior years is erroneous within the meaning of section 452.

(2) Section 452 does not authorize an adjustment if the difference between the treatment accorded an item or transaction in computing the excess profits credit and the treatment accorded such item or transaction in computing the tax liability for prior taxable years is occasioned solely by reason of an adjustment required by a specific provision of the Act, such as the adjustments required by section 433 (b) to normal-tax net income in computing excess profits net income. Since the disallowances under section 451 of deductions on account of expenditures for advertising or the promotion of good will are not required by the Act but are merely permissive at the election of the taxpayer, and since section 451 specifically provides that, if an election is made, the treatment of such expenditures as deductions for prior taxable years shall be considered incorrect, an adjustment under section 452 may be authorized in the case of such a disallowance.

(3) The rule relative to the burden of proof to establish, in any Tax Court or other court proceeding, that an inconsistent position has been taken, is prescribed in section 452 (b) (3). If the net effect of the adjustment by reason of the alleged inconsistency would be an increase in the income taxes previously determined for the prior taxable year or years, the burden of proof is upon the Commissioner. If the net effect of such adjustment would be a decrease in the income taxes previously determined for the prior taxable year or years, the burden of proof is upon the taxpayer. Inasmuch as the adjustment under section 452 is a factor in the determination of the excess profits tax liability, the provisions relative to the burden of proof in a Tax Court or court proceeding do not relieve the taxpayer from responsibility for a full disclosure of the facts necessary to the correct determination of the tax liability.

§ 40.452–3 *Method and effect of adjustment.* (a) The adjustment authorized by section 452, although measured by reference to the income taxes previously determined for prior taxable years, does not operate as an adjustment to the income tax liability for such years, but the amount of such adjustment is added to or subtracted from, as the case may be, the excess profits tax otherwise computed for the taxable year with respect to which the inconsistent position is adopted.

(b) No adjustment with respect to an item or transaction is authorized unless the inconsistent position adopted in the determination is maintained by the party who would be adversely affected by such adjustment. See § 40.452–2 (c). Accordingly, if a determination for one taxable year adopts inconsistent positions with respect to several items or transactions, it is necessary to make separate and distinct computations with respect to each such item or transaction in order to ascertain the amount of the potential adjustment with respect to each such item or transaction and whether an adjustment with respect to such item or transaction is authorized. If several adjustments are authorized with respect to one excess profits tax taxable year, the separate adjustments are aggregated and the aggregate net increase or net decrease is added to, or subtracted from, as the case may be, the excess profits tax otherwise computed for such taxable year. In ascertaining the amount of the adjustment with respect to a particular item or transaction, no effect shall be given to the computations made for the purpose of determining the amount of the adjustment with respect to any other item or transaction. If the several authorized adjustments result in an aggregate net increase, the excess profits tax liability for such taxable year shall not in any case be less than the amount of such aggregate net increase.

(c) If the authorized adjustments with respect to one excess profits tax taxable year result in an aggregate net decrease and the amount of such decrease exceeds the excess profits tax (computed without regard to the provisions of section 452) for such year, the excess may be carried over and subtracted from the excess profits tax in each succeeding taxable year until such excess is exhausted. If excesses result from adjustments with respect to two or more excess profits tax taxable years, such excesses shall be carried over in the order of their occurrence.

(d) The amount of the credit for foreign taxes allowable under the provisions of section 131 shall be determined before giving effect to any adjustment under this section.

§ 40.452–4 *Ascertainment of amount of adjustment* (a) To ascertain the amount of the adjustment, it is necessary to determine the amount of the increase or decrease in each income tax previously determined for each of the prior taxable years which would have resulted if the item or transaction erroneously treated had received the correct treatment under the law applicable with respect to such tax for such year. To each such increase or decrease there shall be added interest thereon computed as if the increase or decrease constituted a deficiency or an overpayment, as the case may be, with respect to such tax for such year. In all such cases interest shall be computed to the 15th day of the third month following the close of the excess profits tax taxable year with respect to which the determination of the excess profits tax liability is made.

(b) If only one income tax for one prior taxable year is involved, the increase or decrease in such tax for such year plus the interest thereon is the amount of the adjustment with respect to the particular item or transaction.

(c) If two or more income taxes for one prior taxable year, or two or more prior taxable years are involved, it is necessary to determine the increase or decrease in each income tax previously determined for each such year, plus the interest on each such increase or decrease. The difference between the sum of the increases, including the interest thereon, and the sum of the decreases, including the interest thereon, shall be ascertained and the net increase or net decrease so determined is the amount of the adjustment with respect to the particular item or transaction.

(d) The computation to determine the increase or decrease in each income tax for each year shall be made as follows:

(1) The amount of the tax previously determined must first be ascertained. This may be the amount of tax shown on the taxpayer's return, but if any changes in that amount have been made they must be taken into account, including any adjustment previously made under the provisions of section 820 of the Revenue Act of 1938 or section 3801 of the Internal Revenue Code. In such cases, the tax previously determined will be the tax shown on the return, increased by the amounts previously assessed (or collected without assessment) as deficiencies, and decreased by amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax. If no amount was shown as the tax on the return, or if no return was made, the tax previously determined will be the sum of the amounts previously assessed (or collected without assessment) as deficiencies, decreased by the amounts previously abated, credited, refunded, or otherwise repaid in respect of such tax.

(2) After the tax previously determined has been ascertained, a recomputation must be made to ascertain the increase or decrease in tax represented by the difference, if any, between the tax previously determined and the tax as recomputed upon the basis of the correct treatment of the item or transaction.

(e) With the exception of the items upon which the tax previously determined was based and the item or transaction with respect to which the erroneous treatment occurred, no item shall be

considered in computing the amount of the increase or decrease in the tax previously determined. If the treatment of any item upon which the tax previously determined was based, or if the application of any provisions of the internal revenue laws with respect to such tax depends upon the amount of income (e. g., charitable contributions or foreign tax credit), readjustment of such items in conformity with the change in the amount of the income which results from the correct treatment of the item or transaction in respect of which the inconsistent position was adopted is necessary as part of the recomputation.

(f) Example: On January 1, 1946, the X Corporation in pursuance of a plan of reorganization transferred all of its assets except cash to the Y Corporation in exchange for all of the stock of the Y Corporation, such stock having a fair market value of $300,000. The assets transferred consisted of depreciable business property acquired by the X Corporation in 1936 which had an adjusted basis in the hands of the X Corporation of $325,000 and an estimated remaining life of 20 years. The fair market value of the property at the time of transfer was $300,000. Both corporations make their returns on the calendar year basis. The exchange was treated as taxable and the loss of $25,000 realized by the X Corporation was recognized. For each of the years 1946 to 1949, inclusive, the Y Corporation was allowed a deduction for depreciation in the amount of $15,000 computed on the cost basis of $300,000. In its income tax return for the calendar year 1950, the Y Corporation claimed that the assets acquired from the X Corporation should have a basis (unadjusted) of $325,000 in determining its invested capital for excess profits tax purposes and claimed a deduction of $16,250 for depreciation on the property for such year. This position was based upon the contention that the 1946 exchange was a nontaxable reorganization resulting from the acquisition by Y Corporation in exchange solely for its voting stock of substantially all of the properties of X Corporation; and that the basis (unadjusted) in the hands of the Y Corporation of the assets acquired upon the exchange was the same as the adjusted basis in the hands of the transferor. Timely claims for refund based upon the allowance of additional deductions for depreciation for the taxable years 1947, 1948, and 1949 were filed. The statute of limitations prevents any refund of overpayments or assessment of deficiencies for the taxable year 1946. The Commissioner's determination of the excess profits tax liability for the calendar year 1950 adopts the inconsistent position asserted by the Y Corporation and, accordingly, if the computation under section 452 (d) discloses a net increase in the taxes previously determined for the taxable year for which correction is prevented, an adjustment is authorized under the provisions of section 452.

The X Corporation's combined normal and surtax for 1946 is $28,500, computed upon normal-tax net income of $75,000 and corporation surtax net income in the same amount. The corporation omitted from the gross income reported on the return an item of rental income amounting to $3,000 and neglected to take a deduction for interest amounting to $1,500. During the taxable year 1946 it realized a gain of $10,000 from the sale of depreciable business property held for more than six months. There was no unused excess profits credit for 1946 which was allowable as a carry-back to a prior taxable year.

The increase in the tax of the X Corporation previously determined for 1946, plus the interest thereon, is computed as follows:

| | |
|---|---|
| Tax previously determined for 1946 | $28,500 |
| Normal tax net income ($75,000) and surtax net income ($75,000) on which tax previously determined was based | 75,000 |
| Plus: Ordinary loss previously allowed under section 117 (j) (excess of $25,000 loss on exchange with Y Corporation over $10,000 gain on sale of other depreciable business property) | 15,000 |
| Ordinary normal-tax net income | 90,000 |
| Ordinary surtax net income | 90,000 |
| Tax as recomputed (38 percent of $80,000 ($90,000 less $10,000 treated as capital gain) plus 25 percent of $10,000 gain from sale of depreciable business property) | 32,900 |
| Tax previously determined | 28,500 |
| Increase in tax | 4,400 |
| Interest on increase in tax | 1,056 |
| Total increase for 1946 | 5,456 |

In accordance with the provisions of section 452 (d), the recomputation does not take into consideration the item of $3,000, representing rental income which was omitted from gross income, or the item of $1,500, representing interest paid, for which no deduction was allowed.

The Y Corporation had normal-tax net income and corporation surtax net income of $100,000 for the taxable year 1946. The decrease in the tax of the Y Corporation previously determined which results solely from the allowance of an additional deduction of $1,250 for depreciation in such year, plus the interest on such decrease, is assumed to be as follows:

| | |
|---|---|
| Tax | $475 |
| Interest | 114 |
| Total | 589 |

The amount of the adjustment to be added to the excess profits tax of the Y Corporation otherwise determined for the taxable year 1950 is as follows:

| | |
|---|---|
| Increase for 1946 (X Corporation) | $5,456 |
| Less: Decrease for 1946 (Y Corporation) | 589 |
| Net increase (amount of adjustment authorized) | 4,867 |

§ 40.452–5 *Interest.* (a) The portion of an adjustment under section 452 which represents interest is characterized as interest for certain tax purposes and is includible in gross income, or allowable as a deduction in computing net income, as the case may be, for the taxable year in which falls the date prescribed for the payment of the excess profits tax for the taxable year to which the adjustment or, in the case of an adjustment involving a carry-over, the portion of such adjustment is applied, regardless of the method of accounting employed by the taxpayer. The date prescribed for payment of the tax is, in the case of a domestic corporation, the 15th day of the third month following the close of the taxable year and, in the case of a foreign corporation not having an office or place of business in the United States, the 15th day of the sixth month following the close of the taxable year.

(b) Under the rule prescribed, if the adjustments in respect of an excess profits tax taxable year result in a net increase, or an aggregate net increase, the portion of such increase which represents interest shall be allowed as a deduction in computing net income for the succeeding taxable year. Thus, under the facts set forth in the example contained in § 40.452–4, the portion of the net increase which represents interest is $942 (interest on the increase, $1,056, minus interest on the decrease, $114), and such interest is allowable as a deduction in computing net income for the calendar year 1951.

(c) If the adjustments in respect of an excess profits tax taxable year result in a net decrease, or an aggregate net decrease, the interest contained in that portion of such decrease which is subtracted from the tax for any taxable year shall be included in the gross income for the succeeding taxable year. For such purpose, no portion of the amount subtracted in any taxable year shall be deemed to represent interest until the portion of the net decrease which represents tax has been exhausted.

(d) Example: For the calendar year 1950, Corporation X had an excess profits tax liability of $9,000 (computed without regard to section 452) and an authorized adjustment under section 452 resulting in a net decrease of $12,000, of which $8,000 represents tax and $4,000 represents interest. In giving effect to the adjustment, $9,000 will be subtracted from the tax for 1950 and the balance will be carried over to succeeding taxable years. Since $8,000 of the net decrease represents tax, only $1,000 of the amount subtracted in 1950 represents interest and hence $1,000 will be included as interest in the taxpayer's gross income for 1951. The entire amount of the $3,000 to be carried over and subtracted from the tax for a succeeding taxable year represents interest, since the portion of the net decrease which represents tax is exhausted in 1950.

SEC. 453. NONTAXABLE INCOME FROM CERTAIN MINING AND TIMBER OPERATIONS, AND FROM NATURAL GAS PROPERTIES.

(a) *Definitions.* For the purposes of this section and section 433 (a)

(1) *Producer; lessor; natural gas company.* The term "producer" means a corporation which extracts minerals from a mineral property, or which cuts logs from a timber block, in which an economic interest is owned by such corporation. The term "lessor" means a corporation which owns an economic interest in a mineral property or

a timber block, and is paid in accordance with the number of mineral units or timber units recovered therefrom by the person to which such property or block is leased. The term "natural gas company" means a corporation engaged in the withdrawal, or transportation by pipe line, of natural gas.

(2) *Mineral unit, natural gas unit, and timber unit.* The term "mineral unit" means a unit of metal, coal, or nonmetallic substance in the minerals recovered from the operation of a mineral property. The term "natural gas unit" means a unit of natural gas sold by a natural gas company. The term "timber unit" means a unit of timber recovered from the operation of a timber block.

(3) *Excess output.* The term "excess output" means the excess of the mineral units, natural gas units, or timber units for the taxable year over the normal output.

(4) *Normal output.* The term "normal output" means the average annual mineral units, or the average annual timber units, as the case may be, recovered in the taxable years beginning after December 31, 1945, and not ending after June 30, 1950 (hereinafter in this section called "normal period"), of the person owning the mineral property or the timber block (whether or not the taxpayer). The term "normal output", in the case of a natural gas company, means the average annual natural gas units sold in the taxable years beginning after December 31, 1945, and not ending after June 30, 1950 (hereinafter in this section called "normal period"), of the person owning the natural gas property (whether or not the taxpayer). The average annual mineral units, natural gas units, or timber units shall be computed by dividing the aggregate of such mineral units, natural gas units, or timber units for the normal period by the number of months for which the mineral property, natural gas property, or timber block was in operation during the normal period and by multiplying the amount so ascertained by twelve. In any case in which the taxpayer establishes, under regulations prescribed by the Secretary, that the operation of any mineral property, natural gas property, or timber block is normally prevented for a specified period each year by physical events outside the control of the taxpayer, the number of months during which such mineral property, natural gas property, or timber block is regularly in operation during a taxable year shall be used in computing the average annual mineral units, natural gas units, or timber units, instead of twelve. Any mineral property, natural gas property, or timber block, which was in operation for less than six months during the normal period, shall, for the purposes of this section, be deemed not to have been in operation during the normal period.

(5) *Natural gas property.* The term "natural gas property" means the property of a natural gas company used for the withdrawal, storage, and transportation by pipe line, of natural gas, excluding any part of such property which is an emergency facility under section 124A.

(6) *Mineral property.* The term "mineral property" means a mineral deposit, the development and plant necessary for the extraction of the deposit, and so much of the surface of the land as is necessary for purposes of such extraction.

(7) *Minerals.* The term "minerals" means ores of the metals, coal, and such nonmetallic substances as abrasives, asbestos, asphaltum, barytes, borax, building stone, cement rock, clay, crushed stone, feldspar, fluorspar, fuller's earth, graphite, gravel, gypsum, limestone, magnesite, marl, mica, mineral pigments, peat, potash, precious stones, refractories, rock phosphate, salt, sand, shell, silica, slate, soapstone, soda, sulphur, and talc.

(8) *Timber block.* The term "timber block" means an operation unit which includes all the taxpayer's timber which would logically go to a single given point of manufacture.

(9) *Normal unit profit.* The term "normal unit profit" means the average profit for the normal period per mineral unit for such period, determined by dividing the net income with respect to minerals recovered from the mineral property (computed with the allowance for depletion computed in accordance with the basis for depletion applicable to the current taxable year) during the normal period by the number of mineral units recovered from the mineral property during the normal period.

(10) *Alternative computation.* In any case in which more than one mineral property is owned or operated by a lessor or producer as defined in (a) (1) of this section, such lessor or producer may treat the mineral properties as one property for purposes of computing exempt excess output under this section.

(11) *Estimated recoverable units.* The term "estimated recoverable units" means the estimated number of units of metal, coal, or nonmetallic substances in the estimated recoverable minerals from the mineral property at the end of the taxable year plus the excess output for such year. All estimates shall be subject to the approval of the Secretary, the determinations of whom for the purposes of this section, shall be final and conclusive.

(12) *Exempt excess output.* The term "exempt excess output" for any taxable year means a number of units equal to the following percentages of the excess output for such year:

100 per centum if the excess output exceeds 50 per centum of the estimated recoverable units;

95 per centum if the excess output exceeds 33⅓ but not 50 per centum of the estimated recoverable units;

90 per centum if the excess output exceeds 25 but not 33⅓ per centum of the estimated recoverable units;

85 per centum if the excess output exceeds 20 but not 25 per centum of the estimated recoverable units;

80 per centum if the excess output exceeds 16⅔ but not 20 per centum of the estimated recoverable units;

60 per centum if the excess output exceeds 14⅔ but not 16⅔ per centum of the estimated recoverable units;

40 per centum if the excess output exceeds 12½ but not 14⅔ per centum of the estimated recoverable units;

30 per centum if the excess output exceeds 10 but not 12½ per centum of the estimated recoverable units;

20 per centum if the excess output exceeds 5 but not 10 per centum of the estimated recoverable units.

(13) *Unit net income.* The term "unit net income" means the amount ascertained by dividing the net income (computed with the allowance for depletion) from the coal or ore or the timber recovered from the mining property, or timber block, as the case may be, during the taxable year by the number of units of coal or ore, or timber, recovered from such property in such year. In respect of a natural gas property, the term "unit net income" means the amount ascertained by dividing the net income, computed in accordance with regulations prescribed by the Secretary, from such property during the taxable year by the number of natural gas units sold in such year.

(b) *Nontaxable income from exempt excess output*—(1) *General rule.* For any taxable year for which the excess output of mineral property which was in operation during the normal period exceeds 5 per centum of the estimated recoverable units from such property, the nontaxable income from exempt excess output for such year shall be an amount equal to the exempt excess output for such year multiplied by the normal unit profit, but such amount shall not exceed the net income (computed with the allowance for depletion) attributable to the excess output for such year.

(2) *Mines in operation during normal period.* For any taxable year, the nontaxable income from exempt excess output of a metal or coal mining property which was in operation during the normal period shall be an amount equal to the excess output of such property for such year multiplied by one-half of the unit net income from such property for such year, or an amount determined under paragraph (1), whichever the taxpayer elects in accordance with regulations prescribed by the Secretary.

(3) *Timber properties.* For any taxable year, the nontaxable income from exempt excess output of a timber block which was in operation during the normal period shall be an amount equal to the excess output of such property for such year multiplied by one-half of the unit net income from such property for such year.

(4) *Mines, timber properties, and natural gas properties not in operation during normal period.* For any taxable year, the nontaxable income from exempt excess output of a metal or coal mining property or a timber block or natural gas property, which was not in operation during the normal period, shall be an amount equal to one-third of the net income for such taxable year (computed with the allowance for depletion) from the metal or coal mining property, the timber block, or the natural gas property, as the case may be. For the purposes of the preceding sentence, a metal mining property shall be deemed not to have been in operation during the normal period if, during the period it was in production during 1946, 1947, 1948, and 1949, the aggregate gross income derived therefrom was less than the aggregate of the deductions (allowed under section 23 without regard to any net operating loss deduction) attributable to such property during such period of production.

(5) *Natural gas companies.* In the case of a natural gas company any of the natural gas property of which was in operation during the normal period, the nontaxable income from exempt excess output for any taxable year shall be an amount equal to the excess output for such year multiplied by one-half of the unit net income for such year.

(c) *Nontaxable bonus income.* The term "nontaxable bonus income" means the amount of the income derived from bonus payments made by any agency of the United States Government on account of the production in excess of a specified quota of:

(1) A mineral product or timber, the exhaustion of which gives rise to an allowance for depletion under section 23 (m), but such amount shall not exceed the net income (computed with the allowance for depletion) attributable to the output in excess of such quota; or

(2) A mineral product extracted or recovered from mine tailings by a corporation which owns no economic interest in the mineral property from which the ore containing such tailings was mined, but such amount shall not exceed the net income attributable to the output in excess of such quota.

(d) *Rule in case income from excess output includes bonus payment.* In any case in which the income attributable to the excess output includes bonus payments (as provided in subsection (c)), the taxpayer may elect, under regulations prescribed by the Secretary, to receive either the benefits of subsection (b) or subsection (c) with respect to such income as is attributable to excess output above the specified quota.

§ 40.453–1 *General rule.* Section 453 provides specific rules for the computation of nontaxable income from exempt excess output which is excluded in the

computation of excess profits net income of (a) a producer of minerals, (b) a producer of logs or lumber from a timber block, (c) a lessor of a mineral property, a coal or metal mining property, or a timber block, or (d) a natural gas company. It also provides specific rules for the computation of nontaxable bonus income of a producer of minerals, or a producer of logs or lumber from a timber block, as defined in such section.

§ 40.453–2 *Definitions.* For the purposes of section 453 and section 433 (a) (1) (I)—

(a) *Producer; lessor; natural gas company*—(1) *Producer.* (i) The term "producer" means a corporation which extracts minerals from a mineral property, or cuts logs from a timber block, in which an economic interest is owned by such corporation. Although section 433 (a) (1) (I) excludes certain nontaxable income in the computation of excess profits net income in the case of a producer of logs or lumber, a producer of lumber is not within the provisions of this subsection unless such corporation is also a producer of the logs from which such lumber is sawed. An economic interest is possessed in every case in which the taxpayer has acquired, by investment, any interest in minerals in place or standing timber and secures, by any form of legal relationship, income derived from the severance and sale of the mineral or timber, to which it must look for a return of its capital. A taxpayer which has no capital investment in the mineral deposit or standing timber does not possess an economic interest merely because, through a contractual relation to the owner, it possesses a mere economic advantage derived from production. Thus, an agreement between the owner of an economic interest and another entitling the latter to purchase the product upon production or to share in the net income derived from the interest of such owner does not convey an economic interest. The mere ownership of the development and plant necessary to the extraction of the minerals in place or the felling and logging of the timber is not an economic interest for the purposes of section 453. Thus, a corporation which owns the equipment necessary to the extraction of minerals or the logging of timber and which acts as an independent contractor or as an agent in extracting minerals or timber, receiving as consideration a portion of the net income from the property, but which does not own an economic interest in the mineral property or timber block is not a producer within the provisions of this paragraph. However, the owner of the economic interest in the mineral property or timber block and from which the mineral or timber is being extracted by the independent contractor or the agent is the producer within the provisions of this paragraph.

(ii) For the purpose of the exclusion from excess profits net income of nontaxable bonus income on account of the production in excess of a specified quota of a mineral product extracted or recovered from mine tailings (see section 453 (c) (2)), a corporation which so extracts or recovers such a mineral product and which owns no economic interest in the mineral property from which the ore containing such tailings was mined shall be deemed to be a producer of minerals.

(2) *Lessor.* The term "lessor" means a corporation which owns an economic interest, as described in subparagraph (1) of this paragraph, in a mineral property, in a metal or coal mining property, or in a timber block, and is paid in accordance with the number of mineral units or timber units recovered from the mineral property, metal or coal mining property, or timber block by the person to which such property is leased. A corporation which leases a mineral property, metal or coal mining property, or a timber block in consideration for the payment, annual or otherwise, of an amount which is not based upon the number of mineral units or timber units recovered from the property or block is not a lessor within the meaning of section 453 (a) (1). However, the fact that the leasehold agreement contains a provision for minimum royalties will not of itself prevent the corporation from being a lessor within the meaning of section 453 (a) (1). Nor does the fact that the corporation which leases a mineral property, metal or coal mining property, or timber block is paid by one who is not a "producer" within the meaning of this section, e. g., an individual to whom such property or block is leased or a lessee which in turn leases the property or block to a sublessee, preclude such corporation from being a lessor within the provisions of section 453 (a) (1), providing it otherwise satisfies the provisions of such section. Likewise, the fact that a corporation which is a lessor within the meaning of section 453 (a) (1) is also a lessee paying rents or royalties to a supervening holder of an economic interest does not prevent such lessor from satisfying the provisions of section 453 (a) (1).

(3) *Natural gas company.* The term "natural gas company" means a corporation which is engaged in the withdrawal of natural gas or the transportation of natural gas by pipeline. It does not include a corporation which is engaged solely in the storage of natural gas or solely in the distribution of natural gas. For the purpose of this paragraph, distribution means the piping of natural gas, which has been received by the distribution facilities either at the end of the pipeline or at some intermediate point along the line, to the ultimate consumers of such gas. A natural gas company need not own an economic interest in the property from which the natural gas is extracted.

(b) *Mineral unit, natural gas unit, and timber unit*—(1) *Mineral unit.* The term "mineral unit" means a unit of metal, coal, or nonmetallic substance in the minerals recovered from the operation of a mineral property. A mineral unit does not mean the number of units of minerals as defined in paragraph (h) of this section but refers to the units of metal, coal, or nonmetallic substances contained in such minerals. If a corporation extracts from the same mineral property two or more minerals containing different metals, coal, or nonmetallic substances, or if two or more metals, coal, or nonmetallic substances are contained in the same mineral extracted by a corporation from a mineral property, a determination of mineral units must be made with respect to each type of metal, coal, or nonmetallic substance contained in such minerals. A unit is any designation of quantity, such as ton, pound, quart, ounce, kilogram, gram, etc., customarily used by the taxpayer as a standard of measurement.

(2) *Natural gas unit.* The term "natural gas unit" means a unit of natural gas sold by a natural gas company. A natural gas unit does not mean a unit of natural gas as extracted or stored but means a unit as sold. A unit is any designation of quantity, such as 1,000 cubic feet, etc., customarily used by the taxpayer as a standard of measurement of sale.

(3) *Timber unit.* The term "timber unit" means a unit of timber recovered from the operation of a timber block. It does not mean the units of lumber, boards, or other wood products sawed from the timber, but refers to the actual logs felled prior to processing at the sawmill. The fact that more than one species of timber is cut by a taxpayer from a timber block shall not be taken into account and a timber unit shall not be established with respect to each species of timber. A unit is any designation of quantity such as board feet measure, log scale, cords, or other units customarily used by the taxpayer as a standard of measurement.

(c) *Excess output.* (1) The term "excess output" means the excess of the mineral units, the natural gas units, or the timber units for the taxable year over the normal output. If the taxpayer operated two or more timber blocks, the excess output shall be determined with respect to each such timber block and shall not be computed upon the basis of the aggregate of the timber blocks owned by the taxpayer. In any case in which more than one mineral property is owned or operated by a lessor or producer, such lessor or producer may treat the mineral properties as one property for purposes of computing exempt excess output. See paragraph (g) of this section. If two or more metals, coal, or nonmetallic substances are contained in the minerals extracted from a mineral property, the determination of the excess output of mineral products extracted from such mineral property for a taxable year shall be made with respect to each separate type of metal, coal, or nonmetallic substance, i. e., the amount by which the mineral units of each type for the taxable year exceeds the normal output of such type. The excess output of a mineral property from which minerals are extracted containing two or more types of metals, coal, or nonmetallic substances shall not be made upon an aggregate basis, i. e., the amount by which the aggregate of all types of mineral units for the taxable year exceeds the aggregate of the normal output of all such types.

(2) The mineral units for a taxable year shall be the number of units of metal, coal, or nonmetallic substances in the minerals recovered from a mineral property during the taxable year, which would be used in computing the

allowance for depletion if the depletion of the mineral property were computed without regard to discovery value or percentage depletion. See § 29.23 (m)–2 of Regulations 111.

(3) The timber units for a taxable year shall be the number of units of timber felled during the year, which is used in the computation of the depletion allowance, but shall not include any timber cut by the taxpayer which owns, or has a contract right to cut, such timber and which has elected pursuant to the provisions of section 117 (k) (1) to treat such cutting as a sale or exchange of the timber as cut. As to the computation of the allowance for depletion, see § 29.23 (m)–21 of Regulations 111.

(4) The number of natural gas units sold during a taxable year shall be the aggregate number of units sold by the natural gas company, whether as a result of withdrawal, of release from storage, or of transportation by pipeline, and regardless of whether different portions of the natural gas property were used in the withdrawal or the transportation of the natural gas sold. Natural gas withdrawn and stored, or transported by pipeline and stored, during the taxable year but not sold during such year shall not be included in the computation of the number of natural gas units for such taxable year for the purpose of the computation of excess output for such year.

(5) The excess output of a lessor shall be computed in the same manner as the excess output of a producer, that is, as the excess of the mineral units or the timber units for the taxable year over the normal output of the mineral property or timber block. The mineral units or timber units of a lessor for the taxable year shall be computed in the same manner as in the case of a producer, except that in the case of a lessor of a timber block there shall not be included in the timber units for such year any timber which has been disposed of by the lessor and which is considered to have been sold under the provisions of section 117 (k) (2). If the disposal of timber by the lessor is not considered a sale of such timber under the provisions of section 117 (k) (2), the number of timber units of the lessor for the taxable year shall not be affected by the fact that the producer of such timber has elected to consider the cutting of such timber as a sale or exchange of such timber cut under section 117 (k) (1).

(d) *Normal output.* (1) The term "normal output" means the average annual mineral units or the average annual timber units recovered, or the average annual natural gas units sold, in the taxable years beginning after December 31, 1945, and not ending after June 30, 1950 (referred to in the regulations under section 453 as the normal period) of the person owning the mineral property, timber block, or natural gas property, whether or not such person is the taxpayer claiming relief under section 433 (a) (1) (I) and section 453. A person includes an individual, a trust, estate, partnership, company, or corporation. See section 3797. If the mineral property or timber block was not owned by the taxpayer for the entire normal period, the taxpayer should, in its first return in which the benefits of section 433 (a) (1) (I) and section 453 are claimed, state the name and address of each person owning the mineral property or timber block during the normal period and submit evidence establishing the mineral units or the timber units recovered from the mineral property or timber block by such other person during the period of its ownership, and the number of months in such period. If all or a portion of the natural gas property owned by the natural gas company during the taxable year was not owned by it during the entire normal period, the taxpayer should, in its first return in which the benefits of section 433 (a) (1) (I) and section 453 are claimed, state the name and address of each person owning such natural gas property, or any portion thereof, during the normal period and submit evidence establishing the natural gas units withdrawn, transported by pipeline, and sold by such other person during the period of its ownership, and the number of months in such period.

(2) In any case in which two or more metals, coal, or nonmetallic substances are contained in the minerals recovered from a mineral property, a normal output shall be computed with respect to each type of metal, coal, or nonmetallic substance in such minerals.

(3) In any case in which a natural gas company withdraws and sells natural gas at the mouth of the well, and in addition transports by pipeline and sells natural gas after such transportation, the normal output shall be computed as the aggregate of the sales prior to and subsequent to transportation.

(4) The average annual mineral units or timber units shall be computed by dividing the aggregate of the mineral units of each type of metal, coal, or nonmetallic substance, or the aggregate of the timber units for the normal period by the number of months for which the mineral property or timber block was in operation during the normal period and by multplying the amount so ascertained by 12. The average annual natural gas units shall be computed by dividing the aggregate of the natural gas units for the normal period by the number of months for which the natural gas property was in operation during the normal period and multiplying the amount so ascertained by 12. In any case in which the taxpayer establishes that the operation of a mineral property, a timber block, or a natural gas property is normally prevented for a specified period each year by physical events outside the control of the taxpayer, the number of months during which such mineral property, timber block, or natural gas property is regularly in operation during a taxable year shall be used in computing the average annual mineral units, or timber units, or natural gas units, instead of 12. If any taxable year for which excess output is computed for the purposes of section 453 is a taxable year of less than 12 months, the number of months in such year, in lieu of 12 and in lieu of the number of months specified in the preceding sentence (if less than such number of months), shall be used in computing the average annual mineral units, timber units, or natural gas units.

(5) The mineral units for a taxable year in the normal period shall be the number of units of each type of metal, coal, or nonmetallic substance in the minerals recovered from a mineral property during the taxable year, which would be used in computing the depletion allowance if the depletion of the mineral property were computed without regard to discovery value or percentage depletion. See § 29.23 (m)–2 of Regulations 111. The timber units for a taxable year shall be the number of units of timber felled during the year used in the computation of the depletion allowance. See § 29.23 (m)–21 of Regulations 111. The natural gas units for a taxable year in the normal period shall be the aggregate of the number of natural gas units withdrawn from, stored in, or transported by, the natural gas property, and sold during such year by the person owning or operating the natural gas property. Natural gas withdrawn and stored, or transported by pipeline and stored, during a taxable year in the normal period but not sold during such year shall not be included in the computation of the number of natural gas units for such year for the purpose of the computation of normal output.

(6) A mineral property, or a timber block, or a natural gas property which was in operation for less than six months during the normal period shall, for the purposes of section 453, be deemed not to have been in operation during the normal period. Such months need not be consecutive months.

(7) The normal output of a lessor shall be computed in the same manner as the normal output of a producer, that is, as the annual average mineral units or the average annual timber units recovered during the normal period of the person owning the mineral property or the timber block. A mineral property or timber block which is owned by a lessor and which was in operation for less than six months during the normal period shall be deemed not to have been in operation during the normal period. Such months need not be consecutive months.

(e) *Natural gas property.* The term "natural gas property" means the entire property of a natural gas company which is used for the withdrawal, storage, and transportation by pipeline of natural gas but does not include any part of such property which is an emergency facility within the provisions of section 124A. As to what constitutes an emergency facility, see section 124A (d) and the regulations thereunder.

(f) *Mineral property.* (1) The term "mineral property" means a mineral deposit, the development and plant necessary for the extraction of the deposit, and so much of the surface of the land as is necessary for the purposes of such extraction. The term "mineral deposit" refers to the minerals in place. The taxpayer's interest in each separate mineral property is a separate "property." If the mineral deposit in which a taxpayer

owns an economic interest extends beyond the boundaries of a single tract or parcel of land, a separate mineral property exists with respect to each tract or parcel of land into which the mineral deposit extends. Where two or more mineral properties are included in a single tract or parcel of land, the taxpayer's interest in such mineral properties may be considered to be a single "property," provided such treatment is consistently followed.

(2) The mineral property of a lessor need not necessarily be coextensive with the mineral property of the producer, but will be determined solely in the light of the economic interest owned by the lessor. For example, a lessor which owns a mineral property as described in this subsection may have leased one-half of such property to one lessee-producer, and the other half to another lessee-producer. The mineral property of each lessee would be limited to that portion of the property leased to it. The mineral property of the lessor would constitute the aggregate of the mineral property leased, unaffected by its subdivision for the purpose of the leasehold agreements. Similarly, an owner of a mineral property may have joined with another owner of an adjacent mineral property in a lease with a lessee in such manner that the lessee acquires a single mineral property. Nevertheless, insofar as the lessors are concerned, each is the owner of a separate mineral property.

(g) *Alternative computation of exempt excess output for more than one mineral property.* Section 453 (a) (10) provides that where more than one mineral property (as defined in paragraph (f) of this section) is owned or operated by a producer or lessor (as defined in paragraph (a) (1) and (2) of this section), such producer or lessor may elect to treat the mineral properties as one property for purposes of computing exempt excess output under section 453. The election shall be made in writing by a statement attached to Schedule EP (Form 1120). In the case of a taxpayer electing under section 453 (a) (10), the allowance for percentage depletion under section 23 (m) shall be computed in a manner consistent with such election for purposes of computing nontaxable income from exempt excess output under section 453 (b).

(h) *Minerals.* The term "minerals" means ores of the metals, coal, and such nonmetallic substances as abrasives, asbestos, asphaltum, barytes, borax, building stone, cement rock, clay, crushed stone, feldspar, fluorspar, fuller's earth, graphite, gravel, gypsum, limestone, magnesite, marl, mica, mineral pigments, peat, potash, precious stones, refractories, rock phosphate, salt, sand, shell, silica, slate, soapstone, soda, sulphur, and talc.

(i) *Timber block.* The term "timber block" means an operation unit which includes all the timber owned by the taxpayer during each year which would logically go to a single given point of manufacture. In those cases in which the point of manufacture is at a considerable distance, or in which the logs or other products will probably be sold in a log or other market, the block may be a logging unit which includes all of the taxpayer's timber which would logically be removed by a single logging development.

The timber block of a lessor need not necessarily be coextensive with the timber block of the producer, but will be determined solely in the light of the economic interest owned by the lessor in the same manner as in the case of a lessor of a mineral property. See paragraph (f) of this section.

(j) *Normal unit profit*—(1) *In general.* (i) The term "normal unit profit" means the average profit for the normal period per mineral unit for such period, determined by dividing the net income with respect to minerals recovered from the mineral property (computed with the allowance for depletion determined in accordance with the basis for depletion, cost basis depletion, discovery value depletion, or percentage depletion, applicable to the current taxable year) during the normal period by the total number of mineral units recovered from the mineral property during the normal period.

(ii) If two or more metals, coal, or nonmetallic substances are contained in the minerals extracted from a mineral property, a normal unit profit shall be established for each class of mineral unit. The normal unit profit for each class of mineral unit shall be determined by dividing the net income with respect to such type of metal, coal, or nonmetallic substance in the minerals recovered from the mineral property during the normal period by the total number of mineral units of such class for the normal period.

(2) *Net income.* (i) Net income with respect to minerals recovered from the mineral property (computed with the allowance for depletion) means the "gross income from the property" as defined in subparagraph (3) of this paragraph less the allowable deductions attributable to the mineral property with respect to which exempt excess output is computed and the allowable deductions attributable to the processes listed in subparagraph (3) of this paragraph insofar as they relate to the product of such property, including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, and including the allowance for depletion. The allowance for depletion shall be computed in accordance with the provisions of section 23 (m) and section 114 (b) and the regulations thereunder. The allowance for depletion for each year during the normal period shall, for the purposes of section 453, be computed upon the same basis used in computing the allowance for depletion during the taxable year for which the benefits of section 453 are claimed. Thus, if during the normal period the taxpayer computed the allowance for depletion with respect to a mineral property upon the cost basis, and if during each taxable year, for which the benefits of section 453 are claimed, the taxpayer computes the allowance for depletion based upon a percentage of income, the allowance for depletion for each year in the normal period shall be recomputed as a percentage of income under the law applicable to each such year. In cases where the taxpayer engages in activities in addition to mineral extraction and to the processes listed in subparagraph (3) of this paragraph, deductions for depreciation, taxes, general expenses, and overhead, which cannot be directly attributed to any specific activity, shall be fairly apportioned between (*a*) the mineral extraction and the processes listed in subparagraph (3) of this paragraph and (*b*) the additional activities, taking into account the ratio which the operating expenses directly attributable to the mineral extraction and the processes listed in subparagraph (3) of this paragraph bear to the operating expenses directly attributable to the additional activities. If more than one mineral property is involved, the deductions apportioned to the mineral extraction and the processes listed in subparagraph (3) of this paragraph shall, in turn, be fairly apportioned to the several properties, taking into account their relative production.

(ii) If two or more metals, coal, or nonmetallic substances are contained in the minerals extracted from a mineral property, a net income with respect to each type of metals, coal, or nonmetallic substance shall be established. Such net income shall be the gross income with respect to such type minus the allowable deductions for such year attributable to such type. The allowable deductions for any taxable year attributable to each type of metal, coal, or nonmetallic substance shall be computed as follows: There shall be determined an amount which bears the same ratio to the total allowable deductions (not including the allowance for depletion) attributable to the mineral property from which the minerals containing such type of metal, coal, or nonmetallic substance has been recovered, as the gross income from such type of metal, coal, or nonmetallic substance bears to the total gross income from such property. To this amount shall be added the allowance for depletion computed with respect to such type of metal, coal, or nonmetallic substance.

(3) *Gross income from the property.* (i) For the purpose of section 453, the term "gross income from the property" for any year in the normal period means the gross income from mining. The term "mining" as used herein includes not only the extraction of ores or minerals from the ground but also the ordinary treatment processes which are normally applied by the mine owners or operators to the crude mineral product after extraction in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the taxpayer establishes to the satisfaction of the Commissioner that the physical and other requirements are such that the ore or minerals must be transported a greater distance to such plants or mills.

(ii) If the taxpayer sells the crude mineral product of the property in the

immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as beneficiated by the ordinary treatment processes actually applied, before transportation of such product. If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes beyond the ordinary treatment processes. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

(iii) The term "ordinary treatment processes," as used in this section, shall include the following:

(*a*) In the case of coal—cleaning, breaking, sizing, and loading for shipment;

(*b*) In the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment;

(*c*) In the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment;

(*d*) In the case of lead, zinc, copper, gold, silver or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation, or by substantially equivalent processes or combination of processes used in the separation of extraction of the product or products from the ore. The furnacing of quicksilver ores is included in the term "ordinary treatment processes." The following processes are not included in the term "ordinary treatment processes": electrolytic deposition, roasting, thermal or electric smelting, refining, or substantially equivalent processes.

(iv) In case any of the ordinary treatment processes are not applied in the immediate vicinity of the mining district in which the mine is located, so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles (unless the taxpayer establishes to the satisfaction of the Commissioner that the physical and other requirements are such that the ore or minerals must be transported a greater distance to such plants or mills) shall be included in the sale price of the product to determine "gross income from the property." Where the plants or mills in which the ordinary treatment processes are applied are in excess of 50 miles from the point of extraction from the ground (and where the taxpayer fails to establish to the satisfaction of the Commissioner that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills) then costs incurred for transportation in excess of 50 miles to the processing location and, if transported by the taxpayer, the proportionate profits attributable to such transportation, should be subtracted from the sale price of the product to determine "gross income from the property." If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

(v) There shall be excluded in determining the "gross income from the property," for each year in the normal period, an amount equal to any rents or royalties which were paid or incurred by the taxpayer in respect of the property and were not otherwise excluded from the "gross income from the property." If royalties in the form of bonus payments were paid in respect of the property in a taxable year in the normal period or any prior years, or if advanced royalties were paid in respect of the property in any taxable year ending prior to December 31, 1939, the amount excluded from "gross income from the property" for a taxable year in the normal period on account of such payments shall be an amount equal to that part of such payments which is allocable to the product sold during the taxable year.

(vi) If the taxpayer paid rents, royalties, or bonuses with respect to the mineral property during the normal period, and in a taxable year for which the benefits of section 453 are claimed owns an economic interest in such property which does not require the payments of rents, royalties, or bonus payments, the amount of such rents, royalties, and bonuses paid during the normal period shall, for the purposes of section 453, not be deducted in the computation of the gross income from the property. If the taxpayer paid rents, royalties, or bonuses with respect to the mineral property during the normal period and in a taxable year for which the benefits of section 453 are claimed pays rents, royalties, or bonuses in amounts different from those paid during the normal period because of a change in its economic interest, the gross income from the property during the normal period shall be recomputed as if the new contractual terms pursuant to which the new rents, royalties, or bonuses are paid had been in effect during the normal period. If the economic interest of the taxpayer during the normal period was such that it did not pay rents, royalties, or bonuses, but such interest has changed so that during the taxable year for which the benefits of section 453 are claimed the taxpayer pays rents, royalties, or bonuses, the gross income from the property during the normal period shall be recomputed as if the contractual agreement pursuant to which rents, royalties, or bonuses are paid during the taxable year were in full force and effect during the normal period. If the economic interest of a person other than the taxpayer in the mineral property during any year in the normal period was different from the economic interest of the taxpayer in the taxable year for which the benefits of section 453 are claimed, the gross income of such person from the property during such normal period year shall be recomputed as if its economic interest in the mineral property were the same as the economic interest of the taxpayer in the taxable year for which the benefits of section 453 are claimed.

(vii) If two or more metals, coal, or nonmetallic substances are contained in the minerals extracted from a mineral property, the gross income from such property shall be allocated to each type of metal, coal, or nonmetallic substance for which a separate mineral unit is established. If the gross income from the property is determined by excluding the costs and proportionate profits attributable to transportation and to processes other than the ordinary treatment processes listed above, or if such gross income is an amount different from the gross proceeds received from the sale of the minerals, the gross income attributable to each type of metal, coal, or nonmetallic substance shall be an amount which bears the same ratio to the gross income from the property which the gross proceeds received from the sale of such type of metal, coal, or nonmetallic substance in the minerals bears to the total gross proceeds received from the sales of all such types.

(viii) In the case of a lessor, the computation of normal unit profit shall be made in a manner similar to that in the case of a producer except that the number of mineral units to be used in the computation of normal unit profit shall be the aggregate of the number of mineral units which were paid for during the normal period. If the lessor's economic interest in the mineral property during the taxable year for which the benefits of section 453 are claimed is different from what it was during the normal period, the gross income of the lessor from the property during the normal period shall be recomputed as if the lessor's economic interest which existed during the taxable year likewise existed in full force and effect during the normal period.

(k) *Estimated recoverable units.* (1) The term "estimated recoverable units" means the estimated number of units of metal, coal, or nonmetallic substances in the estimated recoverable minerals from the mineral property at the end of the taxable year for which the benefits of section 453 are claimed plus the excess output for such year. If the number of

recoverable units of metal, coal, and nonmetallic substances in the minerals in the property have been previously estimated for the prior year or years, and if there has been no known change in the facts upon which the prior estimate was based, the number of recoverable units of metal, coal, and nonmetallic substances in the minerals in the property as of the taxable year will be the number remaining from the prior estimate. Thus, the recoverable units estimated to remain at the end of a taxable year shall be computed, generally, as the estimated recoverable units as of the beginning of the taxable year minus the output for the year. In any case in which it is ascertained either by the taxpayer or the Commissioner as the result of operations or development work prior to the close of the taxable year that the remaining recoverable mineral units are materially greater or less than the number remaining from the prior estimate, the estimate of the remaining recoverable units shall be revised and the revised estimate will be used for the purposes of computing exempt excess output under the provisions of section 453 (a) (12) and (e) of this section unless a change in the facts requires another revision. Regardless of the method of determining the estimated number of units of metal, coal, or nonmetallic substances in the estimated recoverable minerals from the mineral property at the end of the taxable year, the estimated recoverable units for the purposes of section 453 shall be the number of such units plus the excess output for such year. The estimated number of units of metal, coal, or nonmetallic substances in the estimated recoverable minerals means the metal, coal, or nonmetallic substance content of the minerals, and not the estimated recoverable units of the minerals which are the ores of the metals, coal, or nonmetallic substances. The estimated recoverable units from any mineral property shall be determined with respect to each type of metal, coal, or nonmetallic substance in the estimated recoverable minerals and shall not be determined as the aggregate of all classes of mineral units attributable to all such types of metal, coal, or nonmetallic substances. As to the determination of the estimated recoverable units of mineral products, see § 29.23 (m)–9 of Regulations 111.

(2) All estimates of recoverable units of metal, coal, and nonmetallic substances in the estimated recoverable minerals from the mineral property shall be subject to the approval of the Commissioner, and the determination of the Commissioner for the purposes of section 453 shall be final and conclusive.

(l) *Exempt excess output.* (1) The term "exempt excess output" for any taxable year means a number of units equal to the following percentages of the excess output for such year:

100 percent if the excess output exceeds 50 percent of the estimated recoverable units;

95 percent if the excess output exceeds 33⅓ but not 50 percent of the estimated recoverable units;

90 percent if the excess output exceeds 25 but not 33⅓ percent of the estimated recoverable units;

85 percent if the excess output exceeds 20 but not 25 percent of the estimated recoverable units;

80 percent if the excess output exceeds 16⅔ but not 20 percent of the estimated recoverable units;

60 percent if the excess output exceeds 14⅔ but not 16⅔ percent of the estimated recoverable units;

40 percent if the excess output exceeds 12½ but not 14⅔ percent of the estimated recoverable units;

30 percent if the excess output exceeds 10 but not 12½ percent of the estimated recoverable units;

20 percent if the excess output exceeds 5 but not 10 percent of the estimated recoverable units.

(2) Since the excess output and the estimated recoverable units, in the case of a mineral property from which are extracted minerals containing two or more types of metal, coal, or nonmetallic substances, shall be determined with respect to the mineral units comprising the excess output and the mineral units contained in the estimated recoverable units for each separate type of metal, coal, or nonmetallic substance, the percentage which the excess output is of the estimated recoverable units shall be based upon the excess output and the estimated recoverable units of each separate type and shall not be computed with respect to the aggregate of all classes of mineral units. The percentage so determined with respect to each separate type of metal, coal, or nonmetallic substance shall then be multiplied by the excess output of such type of metal, coal, or nonmetallic substance in the minerals recovered from the mineral property, and the product of the two shall be considered the exempt excess output of that type of metal, coal, or nonmetallic substance.

(m) *Unit net income.* (1) The term "unit net income" means the amount of net income per mineral unit of coal or ore or per timber unit for any taxable year for which the benefits of section 453 are claimed. It is ascertained by dividing the net income (computed with the allowance for depletion used in computing net income for normal tax and surtax purposes for such year) from the coal or ore, or the timber, recovered during the taxable year from the mining property, or the timber block, as the case may be, by the number of mineral units contained in the coal or ore recovered from such mining property or by the number of timber units recovered from such timber block, in such year. With respect to a natural gas company, the term "unit net income" means the amount of net income per natural gas unit for any taxable year for which the benefits of section 453 are claimed. It is ascertained by dividing the net income from the natural gas property during such taxable year by the number of natural gas units sold in such year.

(2) For the purpose of section 453 (a) (13) and section 453 (b) (2), a coal mining property shall include the aggregate of all tracts or parcels of land containing coal deposits in which economic interests were owned, and from which coal was extracted, by the taxpayer at any time after the beginning of the normal period (excluding, however, any tract or parcel of land in which an economic interest was acquired, and from which coal was extracted, by any other person subsequent to the last date of ownership and operation by the taxpayer) to the extent that the coal extracted therefrom by the taxpayer was processed at a single preparation plant, regardless of whether the economic interest in one such tract or parcel of land differed from that in another. The coal mining property of a lessor is the tract or parcel of land containing coal deposits in which an economic interest is owned by the lessor. It need not necessarily be coextensive with the coal mining property in the case of the producer.

(3) For the purpose of section 453 (a) (13) and section 453 (b) (2), a metal mining property shall include the aggregate of all tracts or parcels of land containing ore deposits in which economic interests were owned, and from which ore was extracted, by the taxpayer at any time after the beginning of the normal period (excluding, however, any tract or parcel of land in which an economic interest was acquired, and from which ore was extracted, by any other person subsequent to the last date of ownership and operation by the taxpayer) to the extent that such tracts or parcels of land were operated by the taxpayer as an operation unit, regardless of whether the economic interest in one tract or parcel of land differed from that in another. The metal mining property of a lessor is the tract or parcel of land containing ore deposits in which an economic interest is owned by the lessor. It need not necessarily be coextensive with the metal mining property in the case of the producer.

(4) The net income (computed with the allowance for depletion) from the coal or the ore recovered from the mining property during a taxable year for which the benefits of section 453 (b) (2) are claimed shall be the net income from the mining property from which such coal or ore is recovered, computed in a manner similar to that described in paragraph (j) of this section with respect to a mineral property as if such mining property were a mineral property, except that the amount of depletion allowed in the computation of such net income shall be computed according to sections 23 (m) and 114, and the regulations thereunder.

(5) The determination of net income from a timber block for a taxable year must be made with respect to each timber block separately and cannot be made with respect to the aggregate of the timber blocks owned by the taxpayer. Net income from timber recovered from a timber block (computed with the allowance for depletion) means the net income attributable to timber and logging operations, not including transportation of the logs to the log or other market. That portion of the taxpayer's net income attributable to transportation or to manufacturing or remanufacturing, if the taxpayer which is a producer of logs from a timber block carries its operations beyond the logging stage, must be eliminated. If the taxpayer is engaged in activities in addition to timber and logging operations, the net income attributable to timber

recovered from a timber block shall be computed as provided in subparagraph (6) of this paragraph.

(6) Net income from timber recovered from a timber block (computed with the allowance for depletion) means the gross income from the timber block as defined in subparagraph (7) of this paragraph, less the allowable deductions attributable to the timber block with respect to which exempt excess output is computed and the allowable deductions attributable to timbering and logging operations, but not including transportation of the logs to the log or other market, insofar as they relate to logs cut by the taxpayer from the timber block, including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, and including the allowance for depletion. The allowance for depletion shall be that used in computing net income for the taxable year. In cases where the taxpayer engages in activities in addition to timbering and logging operations, including in such additional activities transportation of the logs to the log or other market, deductions for depreciation, taxes, general expenses, and overhead which cannot be directly attributed to any specific activity shall be fairly apportioned between (i) the timber and logging operations, and (ii) the additional activities, taking into account the ratio which the operating expenses directly attributable to the timber and logging operations bear to the operating expenses directly attributable to the additional activities. If more than one timber block is involved, the deductions apportioned to the timber and logging operations shall, in turn, be fairly apportioned to the several timber blocks, taking into account their relative production.

(7) (i) Gross income from the timber block means the amount for which the taxpayer sold the timber or the logs in the immediate vicinity of the timber block, but if the logs were transported or processed or manufactured or remanufactured before sale, it means the representative market or field price (as of the date of sale) of logs of like kind and grade before such transportation, processing, manufacture, or remanufacture. If there was no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any processing, manufacture, or remanufacture (or, if the logs were merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes, manufacture, and remanufacture. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the timber blocks, then such gross income shall be computed by the use of such other method.

(ii) In all cases there shall be excluded in determining the gross income from the timber block an amount equal to any rents or royalties which were paid or incurred by the taxpayer in respect of the timber block and are not otherwise excluded from the gross income from the timber block. If royalties in the form of bonus payments have been paid in respect of the timber block in the taxable year or any prior years or if advanced royalties have been paid in respect of the property in any taxable year ending prior to December 31, 1939, the amount excluded from gross income from the timber block for the current taxable year on account of such payments shall be an amount equal to that part of such payments which is allocable to the product sold during the taxable year. If advanced royalties have been paid in respect of the timber block in any taxable year ending on or after December 31, 1939, the amount excluded from gross income from the timber block for the current taxable year on account of such payments shall be an amount equal to the deduction for such taxable year taken on account of such payments pursuant to the rules provided in § 29.23 (m)–10 (e) of Regulations 111 with respect to advanced royalties paid in the case of mineral properties.

(8) The determination of net income from the natural gas property must be made with respect to the entire natural gas property of the taxpayer as a single property and cannot be made separately with respect to portions of such property. If the natural gas company is engaged in other activities in addition to the withdrawal, storage, and transportation by pipeline of natural gas, the net income from the natural gas company shall not include the income attributable to such other activities. For example, if a natural gas company is engaged in the distribution of natural gas, in addition to the withdrawal, storage, and transportation by pipeline of such gas, that portion of the net income from the sales of the natural gas which is attributable to the distribution of such gas shall not be included in the net income from the natural gas property. For the purposes of this subsection, distribution means the piping of gas, which has been received by the distribution facilities either at the end of a pipeline or at some intermediate point along the line, to the ultimate consumer of such gas. Likewise, the net income from the natural gas property does not include any net income attributable to any portion of the property of the taxpayer which is an emergency facility. So also, income derived from leasing storage facilities to other taxpayers engaged in the withdrawal, or transportation by pipeline, of natural gas shall not be included in the determination of net income from the natural gas property. If the taxpayer derives income from activities other than the withdrawal of natural gas and the transportation of natural gas by pipeline, or is engaged in such withdrawal and transportation by using, in part, property which is not included in the natural gas property, as, for example, an emergency facility, the net income from the natural gas property shall be computed as provided below.

(9) Net income from a natural gas property means the gross income from such property as defined in this subsection less the allowable deductions attributable to such property, including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, and including the allowance for depletion, if any. Any allowance for depletion shall be that used in computing net income for the taxable year. Deductions for depreciation and amortization of operating equipment can be charged directly to natural gas property and other property. Taxes, general expense, and overhead, which cannot be directly attributed to the natural gas property or to other property shall be fairly apportioned between (i) the natural gas property, and (ii) the other property of the taxpayer, taking into account the ratio which the operating expenses directly attributable to the property constituting the natural gas property bears to the operating expenses directly attributable to the other property of the taxpayer.

(10) Gross income from the natural gas property means the aggregate of the gross income received from the sale of natural gas at the mouth of the well or from storage plants in which the natural gas was stored, and from the sale of natural gas at the end of, or at any intermediate point along, the pipeline. It does not include any income derived from the distribution of natural gas after its transportation by pipeline. In the case of a natural gas company which transports natural gas by pipeline to a city and then distributes such gas within the city, the city gate shall be considered the end of the process of transportation by pipeline, and shall be considered the point at which distribution begins. In such a case, the market price at the city gate for the natural gas transported to that point, and subsequently sold, shall be considered to be the gross income from transportation by pipeline of such natural gas. If there is no market price at the city gate or if there is no city gate, the gross income from the natural gas property shall be determined by deducting from the gross income from the sale of such gas the costs and proportionate profits attributable to the local distribution within the city. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the natural gas property, then such gross income shall be computed by the use of such other method.

(11) If any emergency facilities were used in the withdrawal, storage, or transportation of the natural gas, the gross income from the natural gas property shall be the gross income less the costs and proportionate profits attributable to the emergency facilities. Such proportionate profits shall be computed in the same manner as proportionate profits attributable to distribution facilities.

(12) In all cases there shall be excluded in determining gross income from the natural gas property an amount equal to any rents or royalties which were paid or incurred by the taxpayer in respect of the natural gas property and are not otherwise excluded from

the gross income or deducted in computing the net income from the natural gas property. The treatment of royalties in the form of bonus payments or advanced royalties in respect to the natural gas property shall be the same as in the case of such royalties with respect to mineral properties. See paragraph (j) of this section.

(13) The net income from the coal or ore from the mining property, or from the timber block, or from the natural gas property shall be computed with the deduction of any net operating loss deduction attributable to the coal or ore from the mining property, to the timber block, or to the natural gas property. Such net operating loss deduction shall be determined by computing the net operating loss for any taxable year under section 122 (a), the net operating loss carry-overs and carry-backs under section 122 (b), and the adjustment under section 122 (c), as adjusted by section 433 (a) (1) (J), in accordance with the principles of determining net income from the coal or ore from the mining property, from the timber block, or from the natural gas property set forth in this paragraph.

(14) In the case of a lessor of a mining property or a timber block, the computation of unit net income shall be made in a manner similar to that in the case of a producer except that the number of mineral units or timber units to be used in the computation of unit net income shall be the number of mineral units or timber units which were paid for during the taxable year.

§ 40.453–3 *Nontaxable income from exempt excess output.* Nontaxable income from exempt excess output is excluded in the computation of excess profits net income under section 433 (a) (1) (I) and is determined as follows:

(a) *General rule.* (1) If the excess output of a mineral property which was in operation during the normal period exceeds 5 percent of the estimated recoverable units from such mineral property, computed as provided in § 40.453–2 (k) the nontaxable income from exempt excess output shall be an amount equal to the exempt excess output for such year (computed under § 40.453–2 (l)) multiplied by the normal unit profit (computed under § 40.453–2 (j)). In no event shall the amount of nontaxable income from exempt excess output exceed the net income (computed with the allowance for depletion) attributable to the excess output for such year. The net income attributable to excess output shall be that percentage of the net income from the mineral property which the excess output for the taxable year is of the total output for the taxable year. The net income from the mineral property shall be computed in accordance with the rules provided in § 40.453–2 (j) for the computation of net income from the mineral property for a taxable year in the normal period.

(2) If mineral units are determined for two or more tyes of metals, coal, or nonmetallic substances, the nontaxable income shall be determined with respect to the exempt excess output of each type of metal, coal, or nonmetallic substance. In no event shall nontaxable income from exempt excess output be determined with respect to any such type unless the mineral property was in operation during the normal period and unless the excess output of such type exceeds 5 percent of the estimated recoverable units of such type of metal, coal, or nonmetallic substance in the mineral property.

(3) If the minerals recovered from a mineral property contain two or more types of metals, coal, or nonmetallic substances, the nontaxable income from exempt excess output of such property for a taxable year shall be the aggregate of the nontaxable incomes from exempt excess output of each type of metal, coal, or nonmetallic substance. The nontaxable income from exempt excess output of each type of metal, coal, or nonmetallic substance shall be an amount equal to the exempt excess output of such type of metal, coal, or nonmetallic substance (see § 40.453–2 (l) multiplied by the normal unit profit for such type (see § 40.453–2 (j)). The nontaxable income from exempt excess output attributable to each type of metal, coal, or nonmetallic substance shall not exceed the net income (computed with the allowance for depletion) attributable to the excess output of such type for the taxable year. The net income attributable to the excess output of each type of mineral unit shall be determined as follows: The net income attributable to the mineral property for the taxable year shall be fairly allocated to each type of metal, coal, or nonmetallic substance contained in the minerals recovered from the mineral property in such year in accordance with the principles set forth in § 40.453–2 (j). The amount so allocated shall be divided by the total number of mineral units of such type of metal, coal, or nonmetallic substance for the taxable year, and the amount so determined shall be multiplied by the excess output of the mineral units of such type, determined in accordance with § 40.453–2 (c), for the year.

(4) The provisions of this paragraph may be illustrated by the following examples:

*Example (1).* Assume that the taxpayer, which is on the calendar year basis, owns a mineral property from which is extracted a mineral containing one nonmetallic substance. The total output of such property during the four calendar years in the normal period, the first of which began in 1946, was 416,000 tons and the aggregate of the net incomes for such years (including the allowance for depletion computed upon the same basis as for the year 1950) was $1,248,000. The normal output is 104,000 tons and the normal unit profit is $3 per ton. During 1950 minerals containing 200,000 tons of the nonmetallic substance were extracted from the property at a unit profit of $3.50 per ton. The net income for such year was $700,000. As of December 31, 1950, it is estimated that 1,000,000 tons of the nonmetallic substance remained in the mineral property. The amount of nontaxable income from exempt excess output to be excluded in the computation of excess profits net income for 1950 is $57,600, computed as follows:

| | |
|---|---|
| 1. Normal output (tons) | 104,000 |
| 2. Output for 1950 (tons) | 200,000 |
| 3. Excess output for 1950 (tons) | 96,000 |
| 4. Estimated recoverable units for 1950 (1,000,000 tons plus item 3) | 1,096,000 |
| 5. Percentage which item 3 is of item 4 (percent) | 8.8 |
| 6. Percentage of item 3 to be used in computing exempt excess output (percent) | 20 |
| 7. Exempt excess output for 1950 (tons) (item 3 times item 6) | 19,200 |
| 8. Normal unit profit (per ton) | $3.00 |
| 9. Nontaxable income from exempt excess output (item 8 times item 7, but not in excess of item 12) | $57,600.00 |
| 10. Net income or 1950 | $700,000.00 |
| 11. Unit net income for 1950 (per ton) (item 10 divided by item 2) | $3.50 |
| 12. Net income attributable to excess output for 1950 (item 3 times item 11) | $336,000.00 |

*Example (2).* Corporation A, which is on a calendar year basis, owns a mineral property from which it extracts minerals containing gold and silver. The output of silver for each of its four normal period years was 2,500,000 ounces, and of gold was 12,500 ounces. The "gross income from the property" for each normal period year was the sum of the net smelter returns of $1,500,000 received for silver and $437,500 for gold, a total of $1,937,500. Allowable deductions, excluding the allowance for depletion, amounted to $1,000,000. Of the amount of such deductions, $774,193.55 represented the amount allocable to silver production $\left(\frac{1,500,000}{1,937,500} \text{ times } \$1,000,000\right)$ and $225,806.45 represented the amount allocable to gold production $\left(\frac{437,500}{1,937,500} \text{ times } \$1,000,000\right)$. The net income from the mineral property (computed without the allowance for depletion) was $725,806.45 attributable to silver and $211,693.55 attributable to gold. The allowance for percentage depletion computed with respect to silver mining was $225,000 (15 percent of $1,500,000 but not in excess of 50 percent of $725,806.45); the allowance for such depletion computed with respect to gold mining was $65,625 (15 percent of $437,500 but not in excess of 50 percent of $211,693.55). For 1950, the total output of silver was 4,800,000 ounces and of gold was 8,000 ounces. The "gross income from the property" for 1950 was the sum of the net smelter returns of $3,360,000 received for silver and $280,000 received for gold, a total of $3,640,000. Allowable deductions, excluding the allowance for depletion, amounted to $1,280,000. Of the amount of such deductions, $1,181,538.46 represented the amount allocable to silver production $\left(\frac{3,360,000}{3,640,000} \text{ times } \$1,280,000\right)$ and $98,461.54 represented the amount allocable to gold production $\left(\frac{280,000}{3,640,000} \text{ times } \$1,280,000\right)$. The net income from the mineral property (computed without the allowance for depletion) was $2,178,461.54 attributable to silver and $181,538.46 attributable to gold. The allowance for percentage depletion computed with respect to silver mining was $504,000 (15 percent of $3,360,000 but not in excess of 50 percent of $2,178,461.54); the allowance for such depletion computed with respect to gold mining was $42,000 (15 percent of $280,000 but not in excess of 50 percent of $181,538.46). It is estimated that as of December 31, 1950, there were 19,200,000 units of silver and 32,000 units of gold remaining in the mineral property. There is no nontaxable income from exempt excess output of gold, since the normal output exceeds the 1950

output of that metal. The nontaxable income from exempt excess output of silver is $138,220.80, computed as follows:

| | Silver | Gold |
|---|---|---|
| 1. Normal output (ounces): | | |
| a. Silver (10,000,000 divided by 4) | 2,500,000 | |
| b. Gold (50,000 divided by 4) | | 12,500 |
| 2. Output for 1950 (ounces) | 4,800,000 | 8,000 |
| 3. Excess output (item 1a or 1b, minus item 2) | 2,300,000 | 0 |
| 4. Estimated recoverable units as of Dec. 31, 1950 (ounces): | | |
| a. Silver (19,200,000 plus 2,300,000) | 21,500,000 | |
| b. Gold (32,000 plus 0) | | 32,000 |
| 5. Percentage which item 3 is of item 4a or 4b (percent) | 10.7 | |
| 6. Percentage of item 3 to be used in computing exempt excess output (percent) | 30 | |
| 7. Exempt excess output (ounces) (item 3 times item 6) | 690,000 | |
| 8. Normal unit profit per ounce (item 17) | $0.20032 | $11.68548 |
| 9. Nontaxable income from exempt excess output (item 7 times item 8) but not in excess of item 24 | 138,220.80 | 0 |
| *Normal unit profit* | | |
| 10. Gross income from the mineral property for each normal period year | 1,500,000.00 | 437,500.00 |
| 11. Allowable deductions (excluding allowance for depletion) for each normal period year | 774,193.55 | 225,806.45 |
| 12. Net income from the mineral property (excluding allowance for depletion) for each normal period year | 725,806.45 | 211,693.55 |
| 13. Allowance for percentage depletion | 225,000.00 | 65,625.00 |
| 14. Net income from the mineral property for each normal period year | 500,806.45 | 146,068.55 |
| 15. Aggregate net income from the mineral property for the normal period | 2,003,225.80 | 584,274.20 |
| 16. Aggregate mineral units recovered during normal period (ounces) | 10,000,000 | 50,000 |
| 17. Normal unit profit (item 15 divided by item 16) | $0.20032 | $11.68548 |
| *Net income attributable to excess output* | | |
| 18. Gross income from the mineral property for 1950 | 3,360,000.00 | 280,000.00 |
| 19. Allowable deductions (excluding allowance for depletion) for 1950 | 1,181,538.46 | 98,461.54 |
| 20. Net income from the mineral property (excluding allowance for depletion) for 1950 | 2,178,461.54 | 181,538.46 |
| 21. Allowance for percentage depletion | 504,000.00 | 42,000.00 |
| 22. Net income from the mineral property for 1950 | 1,674,461.54 | 139,538.46 |
| 23. Unit net income for 1950 (item 22 divided by item 2) | 0.348846 | 17.4423 |
| 24. Net income attributable to excess output (item 3 times item 23) | 802,345.80 | 0 |

(5) If income attributable to a strategic mineral as defined in section 450 is exempt from the excess profits tax pursuant to the provisions of such section, nontaxable income from exempt excess output of such strategic mineral shall not be computed for the purposes of section 453 (b) (1) or of section 433 (a) (1) (I). The portion of gross income and allowable deductions attributable to such strategic mineral shall be excluded from the net income from the mineral property in determining the net income attributable to other metals or nonmetallic substances in the minerals recovered from such mineral property for the normal period and for the taxable year for which the benefits of sections 453 are claimed.

(*b*) *Metal and coal mines.* (1) The nontaxable income from exempt excess output of a metal or coal mining property which was in operation during the normal period shall be whichever of the following amounts the taxpayer elects—

(i) An amount equal to the the excess output of such metal or coal mining property, determined under this subsection, for such year multiplied by one-half of the unit net income determined under § 40.453–2 (m) from such property for such year, or

(ii) An amount determined under paragraph (a) of this section.

In order to elect the amount provided in subdivision (i) of this subparagraph, the excess output of the metal or coal mining property (as defined in § 40.453–2 (m)) which was in operation during the normal period need not exceed 5 percent of the estimated recoverable units in such property. As to the election with respect to the amount provided in this subdivision, see section 453 (b) (1) and paragraph (a) of this section.

(2) For the purposes of the computation of the amount described in subdivision (i) of subparagraph (1) of this paragraph for a taxable year—

(i) A metal mining property or a coal mining property (as defined in § 40.453–2 (m)) shall be considered to have been in operation during the normal period if any part of such property was in operation for six months or more during the normal period.

(ii) The excess output of a metal mining property or a coal mining property which was in operation during the normal period shall be computed upon the basis of the metal mining property or the coal mining property and shall be the excess of the aggregate of the mineral units extracted from such metal mining or coal mining property during the taxable year over the normal output of such property. The normal output of a metal mining property or a coal mining property shall be computed with respect to such property in a manner similar to that described in § 40.453–2 (d) with respect to a mineral property, as if such metal mining property or coal mining property were a mineral property.

(3) The election pursuant to section 453 (b) and this paragraph shall be made in a statement attached to Schedule EP (Form 1120) accompanying the income tax return, filed on or before the last day required by law for the filing of such return, for the taxable year for which the benefits of section 453 are claimed. The last day required by law for the filing of such return includes the last day of the period of any extension of time granted for such filing. Such election must be made for each taxable year for which the benefits of section 453 (b) (2) are claimed. An election made with respect to a taxable year to compute nontaxable income from exempt excess output pursuant to the provisions of section 453 (b) (2) and subparagraph (1) (i) of this paragraph does not preclude the taxpayer from electing for a subsequent year to compute nontaxable income pursuant to the provisions of section 453 (b) (1) and paragraph (a) of this section provided the taxpayer satisfies the requirements there provided, and vice versa. For any taxable year for which an election is made under section 453 (b) (2) and this paragraph, such election shall be made by the taxpayer by attaching to Schedule EP (Form 1120) a statement showing the method of computation and the amount of nontaxable income from exempt excess output elected under the provisions of section 453 (b) (2) and this paragraph. If the taxpayer has failed so to elect or desires to change its election, such election or change in election may, subject to the approval of the Commissioner, be made by the taxpayer filing with the Commissioner of Internal Revenue, Washington, D. C., within the period of limitations for the filing of claims for credit or refund with respect to the year or years involved, a notice of its election or change in election accompanied by a recomputation of its income and excess profits taxes for such years. If the recomputation results in an overpayment for any of such years, the taxpayer should file a claim for refund on Form 843 in accordance with the provisions of section 322.

(4) The provisions of this paragraph may be illustrated by the following example:

*Example.* Assume that during the taxable year 1950 a corporation owned several tracts of land containing coal deposits which it had operated for more than six months during the normal period. During the taxable year 1950, the coal extracted by the taxpayer from such land was processed at a single preparation plant, so that for the purposes of the computation provided by subparagraph (1) of this paragraph such land constitutes a coal mining property. The normal output of the coal mining property was 350,000 tons. The output for the calendar year 1950 was 450,000 tons. The net income from the coal mining property during 1950 was $103,500. Assume that for the year 1950, the corporation elected to compute an amount of nontaxable income from exempt excess output of the coal mining property under the rule prescribed by subparagraph (1) (i) of this paragraph rather than under subparagraph (1) (ii) of this paragraph. Such amount of nontaxable income from the exempt excess output would be $11,500, computed as follows:

| | |
|---|---|
| 1. Normal output (tons) | 350,000 |
| 2. Output for 1950 (tons) | 450,000 |
| 3. Excess output (tons) (item 2 less item 1) | 100,000 |
| 4. Net income from coal extracted from coal mining property in 1950 | $103,500.00 |
| 5. Unit net income per ton for 1950 (item 4 divided by item 2) | $0.23 |
| 6. Nontaxable income from exempt excess output computed pursuant to section 453 (b) (2) and without regard to section 453 (b) (1) (item 3 times one-half of item 5) | $11,500.00 |

(c) *Timber properties.* (1) The nontaxable income from exempt excess output of a timber block which was in operation during the normal period shall

be an amount equal to the excess output of such timber block for such year, determined under § 40.453–2 (c), multiplied by one-half of the unit net income from such timber block for such year, determined under § 40.453–2 (m).

(2) The provisions of this paragraph may be illustrated by the following example:

*Example.* Assume that the normal unit output of a timber block operated by Corporation T during the normal period was 20,000,000 board feet log scale. The output of timber units for the taxable year 1950 was 32,000,000 board feet log scale and the net income attributable to the timber block, and to timber and logging operations, not including transportation, was $320,000. The nontaxable income from exempt excess output of the timber block for 1950 is $60,000, computed as follows:

| | |
|---|---|
| 1. Normal output (M board feet log scale) | 20,000 |
| 2. Timber units for 1950 (M board feet log scale) | 32,000 |
| 3. Excess output (M board feet log scale) | 12,000 |
| 4. Net income from timber block for 1950 | $320,000 |
| 5. Unit net income per M board feet log scale for 1950 (item 4 divided by item 2) | $10 |
| 6. Nontaxable income from exempt excess output computed pursuant to section 453 (b) (3) (item 3 multiplied by one-half of item 5) | $60,000 |

§ 40.453–4 *Mines, timber properties, and natural gas properties not in operation during normal period.* In the case of a metal mining property, a coal mining property, a timber block, or a natural gas property which was not in operation during the normal period, nontaxable income from exempt excess output is excluded under section 433 (a) (1) (I) in the computation of excess profits net income. For the purposes of the preceding sentence, a metal mining property shall be deemed not to have been in operation during the normal period if, during the period it was in production during 1946, 1947, 1948, and 1949, the aggregate gross income derived therefrom was less than the aggregate of the deductions (allowed under section 23 without regard to any net operating loss deduction) attributable to such property during such period of production. Such nontaxable income from exempt excess output shall be an amount equal to one-third of the net income for the taxable year, computed with the allowance for depletion, from the metal mining property, coal mining property, timber block, or natural gas property as the case may be. Such net income shall be determined in accordance with the provisions of § 40.453–2 (m), relating to unit net income.

§ 40.453–5 *Natural gas companies.* In the case of a natural gas company, as defined in section 453 (a) (1) and section 40.453–2 (a) (3), any portion of the natural gas property of which, as defined in § 40.453–2 (e), was in operation for six months or more during the normal period regardless of whether such portion of such property is in operation during the taxable year, nontaxable income from exempt excess output is excluded in the computation of excess profits net income for any taxable year under section 433 (a) (1) (I). Such nontaxable income from exempt excess output shall be an amount equal to the excess output of such natural gas property for the taxable year determined under § 40.453–2 (c) multiplied by one-half of the unit net income from such natural gas property for such year determined under § 40.453–2 (m).

§ 40.453–6 *Nontaxable bonus income.* (a) The term "nontaxable bonus income" means the amount of the income derived from bonus payments made by any agency of the United States Government on account of the production in excess of a specified quota of either of the following:

(1) A mineral product or timber, if the exhaustion of the mineral property or the timber block from which such product or timber was recovered gives rise to an allowance for depletion under section 23 (m). Such amount, however, shall not exceed the net income (computed with the allowance for depletion) attributable to the output in excess of the quota. Such net income so attributable shall be an amount which bears the same ratio to the net income from the mineral property, computed as provided in § 40.453–2 (j), or the net income from the timber block, computed as provided in § 40.453–2 (m), as the output in excess of the quota bears to the total number of mineral units or timber units produced for the taxable year. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation clearly reflects the net income attributable to the output in excess of the quota, the net income so attributable shall be computed by the use of such other method. If two or more metals, coal, or nonmetallic substances are contained in the minerals recovered from a mineral property, nontaxable bonus income must be determined with respect to each such metal, coal, or nonmetallic substance, and net income from the property must be allocated fairly between each type of metal, coal, or nonmetallic substance. In the case of any such bonus paid with respect to any such type of metal, coal, or nonmetallic substance the nontaxable bonus income shall not exceed the net income attributable to the output in excess of the specified quota of such type. Such net income shall be an amount which bears the same ratio to the net income attributable to such type of metal, coal, or nonmetallic substance as the output in excess of the quota established for such type bears to the number of mineral units of such type produced for the taxable year. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation clearly reflects the net income attributable to the output in excess of the quota established for such type, then the net income so attributable shall be computed by the use of such other method.

(2) A mineral product extracted or recovered from mine tailings by a corporation which does not own an economic interest in the mineral property from which the ore containing such tailings was mined. Such amount, however, shall not exceed the net income attributable to the output in excess of the quota. Such net income so attributable shall be an amount which bears the same ratio to the net income computed with respect to the mineral product extracted or recovered from the tailings as the number of mineral units in the output of the mineral product recovered or extracted from the tailings in excess of the quota bears to the total number of mineral units in the mineral product recovered or extracted from the tailings in the taxable year. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation clearly reflects the net income attributable to the output in excess of the quota, then the net income so attributable shall be computed by the use of such other method. Net income computed with respect to the mineral product extracted or recovered from mine tailings shall be computed pursuant to § 40.453–2 (j), except with respect to the allowance for depletion, as if such mine tailings were a mineral property.

(b) The provisions of this section may be illustrated by the following example:

*Example.* Corporation C, which is on the calendar year basis, owns a mineral property from which it extracts copper ore. The output of copper for each of the four normal period years was 4,380,000 pounds. The 1950 output of copper was 5,500,000 pounds. With respect to Corporation C, a 1950 quota of 4,000,000 pounds of copper was established and a bonus of $0.05 per pound was paid for above quota production. The "gross income from the property" for 1950 was the sum of the net smelter returns, $660,000, and the bonus payments of $75,000, a total of $735,000. Allowable deductions, excluding the allowance for depletion, amounted to $579,700. Net income from the property, without regard to the allowance for depletion, was $155,300. Percentage depletion amounted to $77,650 (15 percent of $735,000 but not in excess of 50 percent of $155,300). As of December 31, 1950, it was estimated that 35,000,000 pounds of copper remained in the mineral property. Since the excess output for 1950 did not exceed 5 percent of the estimated recoverable units for 1950, nontaxable income from exempt excess output is not authorized by section 453 (b) (1). The amount of nontaxable bonus income for 1950 is $21,177 computed as follows:

| | |
|---|---|
| 1. Normal output (pounds) (17,520,000 divided by 4) | 4,380,000 |
| 2. Output for 1950 (pounds) | 5,500,000 |
| 3. Excess output for 1950 (pounds) (item 2 minus item 1) | 1,120,000 |
| 4. Estimated recoverable units for 1950 (pounds) (35,000,000 plus item 3) | 36,120,000 |
| 5. Percentage which item 3 is of item 4 (percent) | 3.1 |
| 6. Gross income for 1950 from the mineral property | $735,000 |
| 7. Allowable deductions (excluding depletion) | 579,700 |
| 8. Net income from the mineral property (excluding depletion) | 155,300 |
| 9. Less percentage depletion | 77,650 |
| 10. Net income for 1950 from the mineral property | 77,650 |
| 11. Unit net income for 1950 (item 10 divided by item 2) | $0.014118 |
| 12. Quota for 1950 (pounds) | 4,000,000 |

| | |
|---|---|
| 13. Above-quota production for 1950 (pounds) (item 2 minus item 12) | 1,500,000 |
| 14. Net income attributable to above-quota production (item 13 times item 11) | $21,177 |
| 15. Bonus payments received | $75,000 |
| 16. Nontaxable bonus income (item 14 or item 15, whichever is the lesser) | $21,177 |

(c) If income attributable to a strategic mineral as defined in section 450 is exempt from excess profits tax pursuant to the provisions of such section, nontaxable bonus income attributable to such strategic mineral shall not be computed for the purposes of section 453 (c) or of section 433 (a) (1) (I). The portion of gross income and allowable deductions attributable to such strategic mineral shall be excluded from the net income from the mineral property in determining the net income attributable to other metals or nonmetallic substances in the minerals recovered from such mineral property for the normal period and for the taxable year for which the benefits of section 453 are claimed.

§ 40.453–7 *Rule in case income from excess output includes bonus payment.* (a) The nontaxable income attributable to exempt excess output pursuant to the provisions of section 453 (b) (1), (2), or (3) may include nontaxable bonus payments, as provided in section 453 (c). In such case, the taxpayer may elect to compute its nontaxable income attributable to the output in excess of the established quota as nontaxable income from exempt excess output pursuant to the appropriate provision of section 453 (b) and § 40.453–3 or as nontaxable bonus income pursuant to section 453 (c) and § 40.453–6. Such election shall be made in a statement attached to Schedule EP (Form 1120) accompanying the income tax return filed prior to the last day prescribed by law for the filing of such return for the taxable year for which the benefits of section 453 are claimed. The last day prescribed by law for the filing of the return includes the last day of the period of any extension granted for such filing. The election provided in section 453 (d) must be made for each taxable year for which income attributable to excess output includes bonus payments. An election made with respect to one taxable year to receive the benefits of nontaxable bonus income under section 453 (c) does not preclude the taxpayer from electing for a subsequent year to receive the benefits of nontaxable income from exempt excess output under section 453 (b), and vice versa. For any taxable year for which an election is made under section 453 (d) and this section, such election shall be made by the taxpayer by attaching to Schedule EP (Form 1120) accompanying its income tax return a statement showing the method of computation and the amount of nontaxable income from exempt excess output under section 453 (b) or of nontaxable bonus income under section 453 (c), whichever the taxpayer elects to exclude under section 433 (a) (1) (I) in the computation of excess profits net income. If the taxpayer has failed so to elect or desires to change its election, such election or change in election may, subject to the approval of the Commissioner, be made in an amended return filed by the taxpayer within the period of limitations for the filing of claims for credit or refund.

(b) The provisions of this section may be illustrated by the following example:

*Example.* Corporation P, which is on the calendar year basis, owns a mineral property from which is extracted minerals containing lead and silver. For each of the four taxable years in the normal period the output of lead was 1,000,000 pounds and of silver was 100,000 ounces. The "gross income from the property" for each year in the normal period was the sum of the net smelter returns of $50,000 received for lead and $70,000 for silver, a total of $120,000. Allowable deductions for each year, excluding the allowance for depletion, amounted to $40,000. Of the amount of such deductions $16,666.67 represented the amount allocable to lead production $\left(\frac{50,000}{120,000} \text{ times } \$40,000\right)$ and $23,333.33 represented the amount allocable to silver production $\left(\frac{70,000}{120,000} \text{ times } \$40,000\right)$. The net income from the mineral property (computed without the allowance for depletion) was $33,333.33 attributable to lead and $46,666.67 attributable to silver. The allowance for percentage depletion computed with respect to lead mining was $7,500 (15 percent of $50,000 but not in excess of 50 percent of $33,333.33); the allowance for such depletion computed with respect to silver mining was $10,500 (15 percent of $70,000 but not in excess of 50 percent of $46,666.67. For 1950, the output of lead was 1,600,000 pounds and of silver was 160,000 ounces. A quota of 900,000 pounds of lead was established with respect to the taxpayer and a bonus of $0.02¾ per pound was paid to the taxpayer with respect to production in excess of such quota. The "gross income from the property" for the year 1950 was $235,250 consisting of $123,250 attributable to lead (the sum of the net smelter returns of $104,000 received for lead and the bonus payment of $19,250 for above-quota production of lead) and $112,000 attributable to silver. Allowable deductions for the year excluding allowance for depletion amounted to $80,000. Of the amount of such deductions, $41,912.86 represented the amount allocable to lead production $\left(\frac{123,250}{235,250} \text{ times } \$80,000\right)$ and $38,087.14 represented the amount allocable to silver production $\left(\frac{112,000}{235,250} \text{ times } \$80,000\right)$. The net income from the mineral property (computed without the allowance for depletion) was $81,337.14 attributable to lead and $73,912.86 attributable to silver. The allowance for percentage depletion computed with respect to lead mining was $18,487.50 (15 percent of $123,250 but not in excess of 50 percent of $81,337.14); the allowance for such depletion computed with respect to silver mining was $16,800 (15 percent of $112,000 but not in excess of 50 percent of $73,912.86). It is estimated that as of December 31, 1950, there were 6,500,000 pounds of lead and 510,000 ounces of silver remaining in the mineral property. For 1950, the amount of nontaxable income from exempt excess output of lead was $3,099.60, the amount of nontaxable bonus income from lead was $19,250, and the amount of nontaxable income from exempt excess output of silver was $6,510.06.

Since the amount of nontaxable bonus income with respect to the output of lead which exceeds the established quota and which also constitutes excess output, i. e., 600,000 pounds, was $16,500 (item 33 in the following computation) and exceeded $3,099.60 representing the nontaxable income from exempt excess output of lead, Corporation P elected under section 453 (d) to exclude $16,500 with respect to such 600,000 pounds in the computation of excess profits net income. With respect to the remaining portion of its output in excess of the established quota, i. e., 100,000 pounds, Corporation P excluded nontaxable bonus income of $2,750 (item 34) in the computation of excess profits net income pursuant to section 453 (c).

COMPUTATION

| | Lead | Silver |
|---|---|---|
| 1. Normal output: | | |
| a. Lead (pounds) (4,000,000 divided by 4) | 1,000,000 | |
| b. Silver (ounces) (400,000 divided by 4) | | 100,000 |
| 2. Output for 1950 | 1,600,000 | 160,000 |
| 3. Excess output (item 2, minus item 1a or 1b) | 600,000 | 60,000 |
| 4. Estimated recoverable units as of Dec. 31, 1950: | | |
| a. Lead (pounds) (6,500,000 plus 600,000) | 7,100,000 | |
| b. Silver (ounces) (510,000 plus 60,000) | | 570,000 |
| 5. Percentage which item 3 is of item 4a or 4b (percent) | 8.45 | 10.53 |
| 6. Percentage of item 3 to be used in computing exempt excess output (percent) | 20 | 30 |
| 7. Exempt excess output (item 3 times item 6) | 120,000 | 18,000 |
| 8. Normal unit profit (item 17) | $0.02583 | $0.36167 |
| 9. Nontaxable income from exempt excess output (item 7 times item 8) but not in excess of item 24 | 3,099.60 | 6,510.06 |
| *Normal unit profit* | | |
| 10. Gross income from the mineral property for each normal period year | 50,000.00 | 70,000.00 |
| 11. Allowable deductions (excluding allowance for depletion) for each normal period year | 16,666.67 | 23,333.33 |
| 12. Net income from the mineral property (excluding allowance for depletion) for each normal period year | 33,333.33 | 46,666.67 |
| 13. Allowance for percentage depletion | 7,500.00 | 10,500.00 |
| 14. Net income from the mineral property for each normal period year | 25,833.33 | 36,166.67 |
| 15. Aggregate net income from the mineral property for the normal period | 103,333.32 | 144,666.68 |
| 16. Aggregate mineral units recovered during the normal period | 4,000,000 | 400,000 |
| 17. Normal unit profit (item 15 divided by item 16) | $0.02583 | $0.36167 |
| *Net income attributable to excess output* | | |
| 18. Gross income from the mineral for 1950 | 123,250.00 | 112,000.00 |
| 19. Allowable deductions (excluding allowance for depletion) for 1950 | 41,912.86 | 38,087.14 |
| 20. Net income from the mineral property (excluding allowance for depletion) for 1950 | 81,337.14 | 73,912.86 |
| 21. Allowance for percentage depletion | 18,487.50 | 16,800.00 |
| 22. Net income from the mineral property for 1950 | 62,849.64 | 57,112.86 |
| 23. Unit net income for 1950 (item 22 divided by item 2) | 0.03928 | 0.35696 |
| 24. Net income attributable to excess output for 1950 (item 3 times item 23) | 23,568.00 | 21,417.6 |

| *Nontaxable bonus income* | *Lead* |
|---|---|
| 25. Quota established for 1950 (pounds) | 900,000 |
| 26. Total output for 1950 (pounds) | 1,600,000 |
| 27. Above-quota output (pounds) | 700,000 |
| 28. Bonus payments received (item 27 times $0.02¾) | $19,250 |
| 29. Net income attributable to above-quota output (item 27 times item 23) | $27,496 |
| 30. Nontaxable bonus income (item 28 or item 29, whichever is the lesser) | $19,250 |

COMPUTATION—Continued

| *Computation of nontaxable income from exempt excess output and from bonus payments with respect to 1950 excess output in excess of quota* | *Lead* |
|---|---|
| 31. Item 3 or item 27, whichever is the lesser | 600,000 |
| 32. Nontaxable income from exempt excess output computed with respect to item 31 (item 9) | $3,099.60 |
| 33. Nontaxable bonus income computed with respect to item 31 (item 31 times $0.02¾) | $16,500.00 |
| 34. Nontaxable bonus income computed with respect to above-quota output in excess of 600,000 pounds, i. e., 100,000 times $0.02¾ (item 30 minus item 33) | $2,750.00 |

SEC. 454. EXEMPT CORPORATIONS.

The following corporations, except a member of an affiliated group of corporations filing a consolidated return under section 141, shall be exempt from the tax imposed by this subchapter:

(a) Corporations exempt under section 101 from the tax imposed by this chapter.

(b) Foreign personal holding companies, as defined in section 331.

(c) Regulated investment companies, as defined in section 361 without the application of section 361 (b) (4).

(d) Personal holding companies, as defined in section 501.

(e) Foreign corporation not engaged in trade or business within the United States.

(f) Domestic corporations satisfying the following conditions:

(1) If 95 per centum or more of the gross income of such domestic corporation for the three-year period immediately preceding the close of the taxable year (or for such part of such period during which the corporation was in existence) was derived from sources other than sources within the United States; and

(2) If 50 per centum or more of its gross income for such period or such part thereof was derived from the active conduct of a trade or business.

(g) Any corporation subject to the provisions of Title IV of the Civil Aeronautics Act of 1938, in the gross income of which for any taxable year ending after June 30, 1950, there is includible compensation received from the United States for the transportation of mail by aircraft if, after excluding from its gross income such compensation, its adjusted excess profits net income for such year is zero or less. Such exclusion from gross income for such year shall also be made in computing the unused excess profits credit adjustment for any other taxable year, but only for the purpose of determining whether the corporation is exempted by this subsection from the tax imposed by this chapter for such other taxable year.

§ 40.454–1 *Exempt corporations.* (a) A corporation which has established its right under section 101 to exemption from income tax (whether or not subject to tax under Supplement U) need not again establish its right under section 454 (a) to exemption from excess profits tax. A corporation which has not established its right to exemption under section 101 and which claims exemption under section 454 (a) is required to establish its right to exemption under section 101 in the manner prescribed in the regulations thereunder in order to be held exempt under section 454 (a).

(b) A corporation which claims exemption under the provisions of section 454, other than the provisions of section 454 (a), (f), and (g), shall file with its return a statement showing under what paragraph of section 454 it claims exemption.

(c) A corporation which claims exemption under section 454 (f) shall attach to its return a statement showing for the 3-year period immediately preceding the close of the taxable year (or for such part thereof during which the corporation was in existence) (1) its total gross income from all sources, (2) the amount thereof derived from the active conduct of a trade or business, (3) a description of such trade or business and the facts upon which the corporation relies to establish that such trade or business was actively conducted by it, and (4) the amount of its gross income from sources within the United States. The gross income from sources within the United States shall be determined as provided in section 119 and the regulations prescribed thereunder.

(d) A corporation which claims exemption under section 454 (g) shall attach to its return for the taxable year for which exemption is claimed a statement showing for such taxable year (1) that it is subject to the provisions of title IV of the Civil Aeronautics Act of 1938, (2) the amount of the compensation included in gross income of the corporation as compensation received from the United States for the transportation of mail by aircraft, and (3) the computation and the amount of its gross income, net income, excess profits net income, excess profits credit, and adjusted excess profits net income, after excluding from its gross income the amount of such compensation received from the United States, including a separate computation of its unused excess profits credit adjustment for such year containing the information required by this subsection with respect to each taxable year entering into the computation of such unused excess profits credit adjustment.

(e) If any corporation described in subsection (d), (f), or (g) of section 454 is a member of an affiliated group of corporations filing a consolidated return under section 141, such corporation shall not be exempt under section 454 for such year.

SEC. 455. RELIEF FOR INSTALLMENT BASIS TAXPAYERS AND TAXPAYERS WITH INCOME FROM LONG-TERM CONTRACTS.

(a) *Election to accrue income.* Any taxpayer computing income from installment sales under the method provided by section 44 (a) or whose principal business consists in purchasing installment sales obligations may elect, in its return for the taxable year, for the purposes of the tax imposed by this subchapter, to compute, in accordance with regulations prescribed by the Secretary, its income from installment sales or installment sales obligations on the basis of the taxable period for which such income is accrued without treating any portion of such income as unrealized at the close of such period in lieu of the basis provided by section 44 (a). Such election shall be irrevocable when once made and shall apply also to all subsequent taxable years to which this subchapter is applicable and the income from installment sales or installment sales obligations for each taxable year before the first year with respect to which the election is made which ended after June 30, 1950, shall be adjusted for the purposes of this subchapter to conform to such election. In making such adjustments, no amount shall be included in computing excess profits net income for any excess profits tax taxable year on account of installment sales made in taxable years ending before July 1, 1950.

(b) *Income from long-term contracts.* Any taxpayer computing income from contracts, the performance of which requires more than 12 months may elect, in its return for the taxable year, for the purposes of the tax imposed by this subchapter, to compute, in accordance with regulations prescribed by the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations and shall be irrevocable when once made, and shall also apply to all subsequent taxable year to which this subchapter is applicable. The net income of the taxpayer for each year to which this subchapter is applicable prior to the year with respect to which the election is made shall be adjusted for the purposes of this subchapter. Income described in this section shall not be considered abnormal income under section 456.

(c) *Adjustment on account of changes with respect to installment basis taxpayers and with respect to taxpayers with income from long-term contracts.* If an adjustment specified in subsection (a) or subsection (b) is, with respect to any taxable year, prevented on the date of the election by the taxpayer under subsection (a) or subsection (b), as the case may be, or within two years from such date, by any provision or rule of law (other than this subsection and other than section 3761, relating to compromises), such adjustment shall nevertheless be made if in respect of the taxable year for which adjustment is sought a notice of deficiency is mailed or a claim for refund is filed, as the case may be, within two years after the date such election is made. If at the time of the mailing of such notice of deficiency or the filing of such claim for refund, the adjustment is so presented, then the amount of the adjustment authorized by this subsection shall be limited to the increase or decrease in the tax imposed by this chapter previously determined for such taxable year which results solely from the effect of subsection (a) or subsection (b), as the case may be, and such amount shall be assessed and collected, or credited or refunded, in the same manner as if it were a deficiency or an overpayment, as the case may be, for such taxable year and as if on the date of such election, two years remain before the expiration of the period of limitation upon the assessment or the filing of claim for refund for the taxable year. The tax previously determined shall be ascertained in accordance with section 452 (d). The amount to be assessed and collected under this section in the same maner as if it were a deficiency or to be refunded or credited in the same manner as if it were an overpayment, shall not be diminished by any credit or set-off based upon any item, inclusion, deduction, credit, exemption, gain or loss, other than one resulting from the effect of subsection (a) or subsection (b), as the case may be. Such amount, if paid, shall not be recovered by a claim or suit for refund, or suit for erroneous refund based upon any item, inclusion, deduction, credit, exemption, gain or loss, other than one resulting from the effect of subsection (a) or subsection (b), as the case may be.

(d) *Cross references.* In the case of a taxpayer making an election under this section—

(1) For adjustment of excess profits net income for taxable years in the base period see section 433 (b) (7) and (8); and

(2) For adjustment in determining the excess profits credit, see section 441 (h).

§ 40.455–1 *Taxpayers reporting income on installment basis; installment sales obligations*—(a) *In general.* Section 455 (a) provides that a corporation which computes income from installment sales under the method provided by section 44 (a), or whose principal

business consists of purchasing installment sales obligations, may elect in its return for the purpose of the excess profits tax to compute its income from installment sales, or installment sales obligations, on the basis of the taxable period for which such income is accrued. No portion of such income shall be treated as unrealized at the close of the period for which the income is accrued. The election shall be made by a statement attached to the return or by the use of figures on the return which clearly reflect the election. The election is irrevocable and applies to all taxable years, including prior and subsequent taxable years, to which the excess profits tax is applicable. If a corporation makes the election, income from installment sales, or installment sales obligations, for each taxable year subject to the excess profits tax must, for the purpose of computing the excess profits tax, be adjusted to conform to such election. No amount, however, will be included in computing excess profits net income for any taxable year ending after June 30, 1950, on account of installment sales made in a taxable year ending before July 1, 1950. A taxpayer electing under section 445 (a) must also (for excess profits tax purposes only) compute its income for all preceding taxable years on the accrual method of accounting. Furthermore, in computing excess profits net income under section 433 (b), the normal-tax net income for the purpose of that section is first recomputed on the accrual method of accounting as if the taxpayer had used that method for all taxable years, and adjustments thereto under section 433 (b) are made in accordance with such recomputation. Except as provided in section 441 (h), if any prior or subsequent year is a factor in computing the excess profits tax, for example, in the case of the net operating loss deduction applicable in computing excess profits net income under section 433 (a) or (b), the computations for such prior or subsequent year are made on the accrual method of accounting. For adjustments in determining invested capital, net new capital addition, the base period capital addition, and the net capital addition or reduction, see section 441 (h). The election under section 455 (a) applies only for the purpose of the excess profits tax; it does not change the method of accounting for the purpose of the normal tax, surtax, etc.

(b) *Definition.* For the purpose of this section, an installment sale means any sale upon credit which the purchaser agrees to repay in two or more scheduled payments, regardless of the maturity of such credit or the amount of the down payment or of each payment, and which for the purposes of the tax imposed by sections 13, 14, and 15 is reported on the installment basis. An installment sale shall not include any casual sale of personal property, and shall not include any sale of real property unless the initial payments received in cash or property (other than evidences of indebtedness of the purchaser) during the taxable period in which the sale is made do not exceed 30 percent of the selling price and unless the taxpayer is regularly engaged in the business of selling real property upon such basis.

(c) *Amended returns.* If a taxpayer makes the election under section 455 (a) in its return for an excess profits tax taxable year other than its first taxable year ending after June 30, 1950, an amended return (including an amended Schedule EP (Form 1120)) shall be filed for each taxable year ending after June 30, 1950, and prior to the taxable year for which the election is made, in order to reflect the effect of computation of income from installment sales, or installment sales obligations, on the accrual method for each such year for purposes of the excess profits tax. If the recomputation produces an overpayment for any of such years, the taxpayer should file a claim for refund on Form 843 with the amended return for such year.

§ 40.455–2 *Computation of income on accrual method.* (a) If the taxpayer has elected under section 455 (a) to compute for excess profits tax purposes its income from installment sales and installment sales obligations on the basis of the taxable year for which such income is accrued, the gross income of the taxpayer from installment sales and installment sales obligations shall be computed upon such accrual basis, and proper adjustment shall be made in computing all deductions and credits of the taxpayer for the taxable year. Thus, all deductions under section 23 allowable in computing net income and attributable to such sales, shall be computed upon the straight accrual basis.

(b) Any deductions under section 23 which are limited to a percentage of net income (computed without regard to such deductions, as for example, the deduction for charitable contributions allowed by section 23 (q)) shall be determined on the basis of such net income with income from installment sales determined upon the accrual method, and not on the basis of such net income for the purposes of the normal tax and surtax. The deduction for bad debts under section 23 (k) shall be allowed only with respect to debts which become worthless within the taxable year. No reserve for bad debts arising from installment accounts receivable may be set up for excess profits tax purposes only, and no bad debt deduction shall be allowed for any additions to such a reserve. Only those debts which have become worthless within the taxable year and which are allowed as a deduction in the computation of net income for the purposes of the normal tax and surtax for the taxable year shall be allowed in the determination of the bad debt deduction for excess profits tax purposes under section 455 (a). If a debt reflected in installment accounts receivable was created in a prior taxable year, and if the total amount of the profit represented by such installment accounts receivable is includible in gross income for such year under the accrual method of accounting, the amount of the deduction for the bad debt shall be computed upon the accrual method and shall not be limited to the unrecovered cost of the goods or articles sold in consideration of such debt.

§ 40.455–3 *Taxpayers with income from long-term contracts*—(a) *In general.* Any corporation computing income from contracts the performance of which requires more than 12 months may elect in its return for the taxable year, for the purpose of the excess profits tax, to compute such income upon the percentage of completion method of accounting. The election shall be made by a statement attached to the return or by the use of figures on the return which clearly reflect the election. The election is irrevocable and applies to all taxable years, including prior and subsequent taxable years, to which the excess profits tax is applicable. If the corporation makes the election, the income from long-term contracts for each year subject to the excess profits tax will, for the purpose of computing the excess profits tax for all taxable years (including prior taxable years), be adjusted to conform to such election. Furthermore, in computing excess profits net income under section 433 (b), the normal-tax net income for the purpose of that section is first recomputed upon the percentage of completion method as if the taxpayer had used that method for all taxable years, and adjustments thereto under section 433 (b) are made in accordance with such recomputation. Except as provided in section 441 (h), if any prior or subsequent year is a factor in computing the excess profits tax, for example, the net operating loss deduction applicable in computing excess profits net income under section 433 (a) or (b), the computations for such prior or subsequent year are made on the percentage of completion method. For adjustments in determining invested capital, the net new capital addition, the base period capital addition, and the net capital addition or reduction, see section 441 (h). The election under section 455 (b) applies only for the purpose of the excess profits tax; it does not change the method of accounting for the purpose of the normal tax, surtax, etc.

(b) *Amended returns.* If the taxpayer makes the election under section 455 (b) in its return for an excess profits tax taxable year other than its first taxable year ending after June 30, 1950, an amended return (including an amended Schedule EP (Form 1120)) shall be filed for each taxable year ending after June 30, 1950, and prior to the taxable year for which the election is made, in order to reflect the effect of computation of income from long-term contracts, for purposes of the excess profits tax, for such years on the percentage of completion method of accounting. If the recomputation produces an overpayment for any of such years, the taxpayer should file a claim for refund on Form 843 with the amended return for such year.

§ 40.455–4 *Computation of net income upon percentage of completion method of accounting*—(a) *Excess profits tax taxable year.* If a taxpayer has elected under section 455 (b) to compute for excess profits tax purposes its net income from long-term contracts upon the percentage of completion method of accounting, gross income from such long-

term contracts shall be reported for each excess profits tax taxable year upon the basis of percentage of completion of such contract in such year. Except as provided in section 441 (h), this is true wherever income is a factor in determining the excess profits tax and applies not only to the taxable year for which the excess profits tax is being determined but also to all prior and subsequent years which affect the excess profits tax liability for such year. There shall be deducted from such gross income for the taxable year all expenditures made during such year on account of the contract, account being taken of the material and supplies on hand at the beginning and end of the taxable year for use in connection with the work under the contract but not yet so applied. Any deductions under section 23 which are limited to a percentage of net income (computed without regard to such deduction, as for example, the deduction for charitable contributions which is allowed by section 23 (q) shall, for excess profits tax purposes, be determined upon the basis of such net income with the income from long-term contracts computed upon the percentage of completion method of accounting, and not upon the basis of net income for purposes of the normal tax and surtax. No reserve for bad debts arising from accounts receivable from long-term contracts may be set up for excess profits tax purposes unless a reserve has been established for income tax purposes.

(b) *Taxable year in the base period.* If a taxpayer elects, pursuant to section 455 (b), to compute its income from long-term contracts upon the percentage of completion method of accounting, the excess profits net income for a taxable year in the base period to be used in computing the average base period net income shall be computed pursuant to section 433 (b) but with income from long-term contracts computed upon the percentage of completion method of accounting as described in paragraph (a) of this section in lieu of the completed contract method. In such event gross income attributable to each long-term contract shall be placed in the appropriate year in the base period upon the percentage of completion method of accounting, regardless of whether such contract was completed in a subsequent year in the base period or in an excess profits tax taxable year and regardless of when gross income from such contract was reported for purposes of the normal tax and surtax. Likewise, gross income attributable to each long-term contract completed during a taxable year in the base period shall be included in income for such year only to the extent to which such income is attributable to the percentage of the contract completed in such year. Gross income attributable to the percentage of the contract completed prior to the base period shall be excluded in the computation of excess profits net income for a taxable year in the base period and consequently from average base period net income. There shall be deducted from such gross income for each taxable year in the base period all expenditures made during the taxable year on account of the contract, account being taken of the material and supplies on hand at the beginning and end of each year for use in connection with the work under the contract but not yet so applied.

§ 40.455–5 *Adjustment on account of change arising under section 455 (a) or section 455 (b).* (a) If the adjustment of the tax imposed for any taxable year, in order to give effect to the recomputations provided under section 455 (a) (in the case of a taxpayer with income from installment sales or installment sales obligations) or under section 455 (b) (in the case of a taxpayer with long-term contracts), is prevented on the date of the election by the taxpayer under section 455 (a) or section 455 (b), as the case may be, or within two years from such date by any provision of law (other than section 455 and other than section 3761, relating to compromises) or by any rule of law, including the doctrine of res judicata, an adjustment under section 455 (c) shall nevertheless be made if with respect to the taxable year for which such adjustment is sought a notice of deficiency is mailed or a claim for refund is filed, as the case may be, within two years after the date such election was made. Section 455 (c) applies only if at the time of filing of a claim for refund or the mailing of the notice of the deficiency the adjustment would otherwise be prevented by the running of the statute of limitations, by the execution of a closing agreement, by the operation of the rule of res judicata, or because of other reasons. For reference to provisions which would prevent adjustment except for the provisions of section 455 (c), see § 29.3801 (b)–0 of Regulations 111. Section 455 (c) is not applicable if, on the date of the filing of the claim for refund or the mailing of the notice of deficiency, adjustment of the tax liability is permissible without recourse to such section.

(b) The amount of the adjustment authorized by section 455 (c) is limited to the increase or decrease in the tax imposed previously determined for the taxable year which results solely from the revision of the excess profits tax liability effectuated by section 455 (a) or section 455 (b), as the case may be, and the collateral effects of such revision upon items of income, deductions, credits, average base period net income, etc., already taken into account in ascertaining the tax previously determined. The tax previously determined shall be ascertained in accordance with section 452 (d). If the amount of the adjustment determined under section 455 (c) represents an increase in tax, it is to be treated in the same manner, and assessed and collected as if it were a deficiency for the taxable year; if the amount of the adjustment represents a decrease in tax, it is to be treated, credited, or refunded, in the same manner as if it were an overpayment for the taxable year. In either case the increase or decrease shall be treated as if on the date of the election pursuant to section 455 (a) or section 455 (b), as the case may be, two years remain before the expiration of the period of limitation upon assessment or the filing of a claim for refund for the taxable year. The amount of the adjustment considered as a deficiency or as an overpayment, as the case may be, will bear interest to the extent provided by the internal revenue laws applicable to deficiencies and overpayments for the taxable year for which the adjustment is made.

(c) The amount of any adjustment under section 455 (c) to be collected in the same manner as if it were a deficiency and the amount of any adjustment to be refunded or credited in the same manner as if it were an overpayment, as the case may be, shall not be diminished by any credit or set-off based upon any item, inclusion, deduction, credit, exemption or gain or loss other than one resulting from the effect of section 455 (a) or section 455 (b), as the case may be.

(d) The amount of any adjustment under the provisions of section 455 (c) which is refunded may not subsequently be recovered in a suit for erroneous refund based upon any adjustment other than one resulting from the revision of excess profits tax liability occasioned by the recomputation of tax pursuant to an election under section 455 (a) or section 455 (b), as the case may be. The amount of any adjustment under section 455 (c) which is assessed and collected as a deficiency may not thereafter be recovered by the taxpayer in any suit for refund based upon any adjustment other than one resulting from the revision of excess profits tax liability occasioned by the recomputation of tax pursuant to an election under section 455 (a) or section 455 (b), as the case may be.

SEC. 456. ABNORMALITIES IN INCOME IN TAXABLE PERIOD.

(a) *Definitions.* For the purposes of this section—

(1) *Abnormal income.* The term "abnormal income" means income of any class described in paragraph (2) includible in the gross income of the taxpayer for any taxable year under this subchapter if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 115 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence.

(2) *Separate classes of income.* Each of the following subparagraphs shall be held to describe a separate class of income:

(A) Income arising out of a claim, award, judgment, or decree, or interest on any of the foregoing; or

(B) Income resulting from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months; or

(C) Income from the sale of patents, formulae, or processes, or any combination of the foregoing, developed over a period of more than 12 months; or

(D) Income includible in gross income for the taxable year rather than for a different taxable year by reason of a change in the taxpayer's method of accounting.

All the income which is classifiable in more than one of such subparagraphs shall be classified under the one which the taxpayer irrevocably elects. The classification of income of any class not described in subparagraphs (A) to (D), inclusive, shall be subject to regulations prescribed by the Secretary.

(3) *Net abnormal income.* The term "net abnormal income" means the amount of the abnormal income less, under regulations prescribed by the Secretary, (A) 115 per centum of the average amount of the gross income of the same class determined under paragraph (1), and (B) an amount which bears the same ratio to the amount of any costs or deductions relating to such abnormal income, allowable in determining the normal-tax net income for the taxable year, as the excess of the amount of such abnormal income over 115 per centum of such average amount bears to the amount of such abnormal income.

(b) *Amount attributable to other years.* The amount of the net abnormal income that is attributable to any previous or future taxable year or years shall be determined under regulations prescribed by the Secretary. In the case of amounts otherwise attributable to future taxable years, if the taxpayer either transfers substantially all its properties or distributes any property in complete liquidation, then there shall be attributable to the first taxable year in which such transfer or distribution occurs (or if such year is previous to the taxable year in which the abnormal income is includible in gross income, to such latter taxable year) all amounts so attributable to future taxable years not included in the gross income for a previous taxable year.

(c) *Computation of tax for current taxable year.* The tax under this subchapter for the taxable year, in which the whole of such abnormal income would without regard to this section be includible, shall not exceed the sum of:

(1) The tax under this subchapter for such taxable year computed without the inclusion in gross income of the portion of the net abnormal income which is attributable to any other taxable year, and

(2) The aggregate of the increase in the tax under this subchapter for the taxable year (computed under paragraph (1)) and for each previous taxable year which would have resulted if, for each previous taxable year to which any portion of such net abnormal income is attributable, an amount equal to such portion had been included in the gross income for such previous taxable year.

(d) *Computation of tax for future taxable year.* The amount of the net abnormal income attributable to any future taxable year shall, for the purposes of this subchapter, be included in the gross income for such taxable year.

(1) The tax under this subchapter for such future taxable year shall not exceed the sum of—

(A) The tax under this subchapter for such future taxable year computed without the inclusion in gross income of the portion of such net abnormal income which is attributable to such year; and

(B) The decrease in the tax under this subchapter for the previous taxable year in which the whole of such abnormal income would, without regard to this section, be includible which resulted by reason of the computation of such tax for such previous taxable year under the provisions of subsection (c); but the amount of such decrease shall be diminished by the aggregate of the increases in the tax under this subchapter for the future taxable year as computed under subparagraph (A) and for the taxable years intervening between such previous taxable year and such future taxable year which have resulted because of the inclusion of the portions of such net abnormal income attributable to such intervening years in the gross income for such intervening years.

(2) If, in the application of subsection (c), net abnormal income from more than one taxable year is attributable to any future taxable year, paragraph (1) of this subsection shall be applied with respect to such future taxable year in the order of the taxable years from which the net abnormal income is attributable beginning with the earliest, as if the portion of the net abnormal income from each such year was the only amount so attributable to such future taxable year, and (except in the case of the portion for the earliest previous taxable year) as if the tax under this subchapter for the future taxable year was the tax determined under paragraph (1) with respect to the portion for the next earlier previous taxable year.

(3) If in the application of paragraph (1) to any future taxable year it is determined that the decrease in tax computed under paragraph (1) (B) with respect to the net abnormal income, a portion of which is included in the gross income for the future taxable year, does not exceed the aggregate of the increases in tax computed under paragraph (1) (B) with respect to such net abnormal income, then the portions of such net abnormal income attributable to taxable years subsequent to such future taxable year shall not be included in the gross income for such subsequent taxable year. For the purpose of computing the tax under this subchapter for a taxable year subsequent to the future taxable year, the portion of net abnormal income attributable to the future taxable year shall not be included in the gross income for such future taxable year to the extent that the inclusion of such portion of net abnormal income in the gross income for such future taxable year did not result in an increase in tax for such future taxable year by reason of the provisions of paragraph (1).

(e) *Application of section.* This section shall be applied only for the purpose of computing the tax under this subchapter as provided in subsections (c) and (d), and shall have no effect upon the computation of base period net income. For the purposes of subsections (c) and (d)—

(1) Net abnormal income means the aggregate of the net abnormal income of all classes for one taxable year.

(2) Under regulations prescribed by the Secretary, the tax under this subchapter for previous taxable years shall be computed as if the portions of net abnormal income for each previous taxable year for which the tax was computed under this section were included in the gross income for the other previous taxable years to which such portions were attributable.

(3) If both subsections (c) and (d) are applicable to any current taxable year, subsection (d) shall be applied without regard to subsection (c), and subsection (c) shall be applied as if the tax under this subchapter, except for subsection (c), was the tax computed under subsection (d) and as if the gross income and the other amounts necessary to determine the adjusted excess profits net income were those amounts which would result in the tax computed under subsection (d).

§ 40.456–1 *Abnormalities in income in taxable year.* (a) Section 456 applies if abnormal income (as defined in section 456 (a)) for any excess profits tax taxable year is attributable to other taxable years. The term "abnormal income" means income of any class described in § 40.456–2 includible in the gross income of the taxpayer for any excess profits tax taxable year (1) if it is abnormal for the taxpayer to derive gross income of such class, or (2) if the taxpayer normally derives gross income of such class but the amount of such income of such class is in excess of 115 percent of the average amount of the gross income of the same class determined for the four previous taxable years or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence. It is abnormal for a taxpayer to derive income of any class only if the taxpayer had no gross income of that class for the four previous taxable years. For the purpose of determining abnormal income under this paragraph the gross income of the class for the previous taxable years is not to be increased or decreased by any allocation under the provisions of section 456. Abnormal income is to be determined by considering classes of income, and not merely particular items.

(b) Abnormal income must be adjusted, as provided in section 456 (a) (3), in order to determine net abnormal income. Net abnormal income must then be allocated to the various items included in abnormal income. The items of net abnormal income so determined are the amounts which may be attributed to other taxable years under these regulations. Net abnormal income and the allocated amounts which are items of net abnormal income are determined in the manner provided in paragraphs (c) and (d) of this section.

(c) Net abnormal income is determined as follows:

(1) The abnormal income of each class is computed;

(2) Such abnormal income is then reduced by 115 percent of the average amount of the gross income of the same class for the four previous taxable years or, if the taxpayer was not in existence for four previous taxable years, the previous taxable years during which it was in existence;

(3) The abnormal income is further reduced by an amount which bears the same ratio to the amount of any costs or deductions relating to such abnormal income, allowable in determining the normal-tax net income for the taxable year, as the abnormal income, reduced as provided in subparagraph (2), of this paragraph, bears to the abnormal income. The amount thus determined is the net abnormal income.

(d) The items of net abnormal income are determined as follows:

(1) Each item of abnormal income is reduced, but not below zero, by an amount equal to 115 percent of the average income, if any, for the four previous taxable years, arising out of the same property as the income represented by the item;

(2) Each item of abnormal income is further reduced, but not below zero, by an amount which bears the same ratio to the amount of any costs or deductions relating to such abnormal income, allowable in determining the normal-tax net income for the taxable year, as the amount of the item of abnormal income reduced in subparagraph (1) of this paragraph, bears to the amount of the item of abnormal income;

(3) The aggregate of the items as reduced under subparagraph (1) of this paragraph and (2) is determined;

(4) Net abnormal income is allocated to each item in the proportion that the item, reduced as provided in subparagraphs (1) and (2) of this paragraph, bears to the aggregate of the items so reduced, determined in subparagraph (3) of this paragraph. The amount so allocated is an item of net abnormal income.

(e) Example: For the taxable year 1950, the A Corporation, which makes its income tax returns on the calendar year basis, has gross income of $1,000,000 from judgments. This consists of two items, one of $800,000 for a judgment against X and the other of $200,000 for a judgment against Y. Its average income of this class for the four previous taxable years was $300,000. For 1950, it has deductible expenses of $160,000 applicable to the judgment against X. There were no deductible expenses applicable to the other judgment. The $1,000,000 is abnormal income, since it is in excess of 115 percent of the average income of this class for the four previous taxable years. The items of net abnormal income represented by the judgment are determined as follows:

| | | |
|---|---|---|
| (1) Abnormal income | | $1,000,000 |
| (2) Less 115 percent of average income ($300,000) for the four previous taxable years | | 345,000 |
| (3) Excess of (1) over (2) | | 655,000 |
| (4) Less an amount bearing same ratio to $160,000 (deductions applicable to items in this class) as $655,000 bears to $1,000,000 | | 104,800 |
| (5) Net abnormal income | | 550,200 |
| (6) Gross income on account of the judgment against X | $800,000 | |
| (7) Less deductions applicable to such item | 160,000 | |
| (8) Amount of (6) reduced by (7) | | 640,000 |
| (9) Gross income on account of the judgment against Y | $200,000 | |
| (10) Less deductions applicable to such item | None | |
| (11) Amount of (9) reduced by (10) | | 200,000 |
| (12) Aggregate of (8) and (11) | | 840,000 |
| (13) Portion of net abnormal income allocated to the judgment against X (640,000/840,000 of $550,200) | | 419,200 |
| (14) Portion of net abnormal income allocated to the judgment against Y (200,000/840,000 of $550,200) | | 131,000 |

§ 40.456–2 *Classification of income.* (a) Section 456 (a) (2) (A), (B), (C), and (D) sets forth four separate classes of income. All the income which reasonably is classifiable in more than one class shall be classified under the one which the taxpayer irrevocably elects. Such election shall be made in the manner prescribed in § 40.456–3. The classification of income for any year must be consistent with the classification made under section 456 for previous years. The classification must also be consistent with any classification made in applying section 433 (b) (9) to the taxpayer.

(b) Other income, not within a class described in subparagraphs (A)–(D) of section 456 (a) (2), to which section 456 is applicable may be grouped by the taxpayer, subject to approval by the Commissioner on the examination of the taxpayer's return, in such classes similar to those specified in subparagraphs (A)–(D) of section 456 (a) (2) as are reasonable in a business of the type which the taxpayer conducts, and as are appropriate in the light of the taxpayer's business experience and accounting practice.

§ 40.456–3 *Amount attributable to other years.* (a) The mere fact that an item includible in gross income is of a class abnormal either in kind or in amount does not result in the exclusion of any part of such item from excess profits net income. It is necessary that the item be found attributable under the regulations in this part in whole or in part to other taxable years. Only that portion of the item which is found to be attributable to other years may be excluded from the gross income of the taxpayer for the year for which the excess profits tax is being computed.

(b) Items of net abnormal income are to be attributed to other years in the light of the events in which such items had their origin, and only in such amounts as are reasonable in the light of such events. To the extent that any items of net abnormal income in the taxable year are the result of such factors as high prices, low operating costs, increased demand, or decreased competition, such items shall not be attributed to other taxable years. Thus, no portion of an item is to be attributed to other years if such item is of a class of income which is in excess of 115 percent of the average income of the same class for the four previous taxable years solely because of an improvement in business conditions. In attributing items of net abnormal income to other years, particular attention must be paid to changes in those years in the factors which determined the amount of such income. No portion of an item of net abnormal income is to be attributed to any previous year solely by reason of an investment by the taxpayer in assets, tangible or intangible, employed in or contributing to the production of such income.

(c) Section 456 has no effect upon the computation of base period net income or of earnings and profits and therefore does not affect the computation of the excess profits credit. Similarly, it has no application in the determination of taxes other than the excess profits tax imposed by subchapter D of chapter 1 (except where the excess profits tax is applicable in the computation of other taxes). Amounts attributed to future years are to be included in gross income for such years for excess profits tax purposes only. If the taxpayer either transfers substantially all its properties or distributes any property in complete liquidation prior to the close of the last future taxable year to which any such amounts are attributable, then all amounts of net abnormal income attributable to years subsequent to both—

(1) The first taxable year in which such transfer or distribution in liquidation occurs, and

(2) The taxable year in the gross income of which such abnormal income would have been included except for section 456

shall be included in the gross income for the year referred to in (1) or the year referred to in (2), whichever is the later. For example, if a taxpayer realizes in 1951 net abnormal income attributable to the years 1950 to 1953, inclusive, and in 1952 begins to distribute its property in complete liquidation, the portion of the net abnormal income attributable to the future year 1953 is to be reallocated to and included in the gross income for 1952 (the first year of liquidation) in addition to the amount already attributed to that year. If the first distribution in liquidation occurred before the year of realization, for example, in 1950, the portions of the net abnormal income attributable to the future years 1952 and 1953 would be included in the gross income for 1951 (the year of realization) in addition to the amount already attributed to that year. In neither event will the allocation originally made to 1950 and 1951 be disturbed.

(d) A taxpayer claiming the benefits of section 456 shall file with its excess profits tax return a detailed statement in duplicate containing the following information:

(1) The amount and a description of each class of income claimed to be abnormal, and the amount and a description of each item in each such class;

(2) For each class of income claimed to be abnormal, the amount and a description of each item of income of the same class derived during the four taxable years, immediately preceding the taxable year, and the aggregate amount of such items for each taxable year;

(3) For each class of income claimed to be abnormal, the amount of net abnormal income, the amount of each item of net abnormal income, and the computations by which these amounts were determined;

(4) The transactions in which each such item had its origin, the method used in allocating such item, the amount allocated to each year, and the reasons therefor; and

(5) All other facts upon which the taxpayer relies.

If any item of income is reasonably classifiable in more than one class, the inclusion of such item in any one of such classes in the statement referred to above shall constitute an irrevocable election by the taxpayer for the purpose of section 456 (a) (2).

§ 40.456–4 *Computation of tax for current taxable year.* (a) The excess profits tax for the taxable year shall be the smaller of the following amounts:

(1) The excess profits tax computed without excluding from gross income any amounts attributable to other years under section 456, and so computed with the application of section 456 (d), relating to the tax for future taxable years to which net abnormal income is attributable, if such section is applicable to such taxable year; or

(2) The sum of (i) the excess profits tax for the taxable year computed without including in gross income the amount of items of net abnormal income attributable to other taxable years

and so computed with the application of section 456 (d) if such section is applicable, and (ii) the aggregate of the amounts of additional excess profits tax which would have resulted for the taxable year in the computations under subdivision (i) of this subparagraph and for each previous excess profits tax taxable year if there had been included in the gross income for each previous taxable year the amount of the items, if any, of the net abnormal income attributable thereto. If the excess profits tax for any previous taxable years was computed under section 456, the increases in tax under subdivision (ii) of this subparagraph shall be computed on the basis of the computations made for such previous taxable years, that is, as if the gross income for all previous taxable years included the items of net abnormal income attributable to such previous taxable years from the other previous taxable years to which section 456 applied.

(b) Since the net abnormal income attributable to any taxable year, if included in the gross income for such taxable year, would reduce items, such as the net operating loss or unused excess profits credit, for such year which are taken into account in other taxable years through a carry-over or carry-back, such inclusion in gross income may also result in an increase in tax in such other taxable years in which such loss or unused credit is taken into account in computing the net operating loss deduction or unused excess profits credit adjustment. Section 456 requires that the increase in tax for the taxable year in which such net operating loss deduction or unused excess profits credit adjustment would be affected by the attributed income must be taken into account in computing the tax under section 456. Such income shall not be included in determining the net abnormal income for the taxable year to which it is attributable. The increase in tax caused by any adjustment under section 456 is the difference between the tax computed without such adjustment and the tax computed after making such adjustment.

(c) The computations required by sections 456 (c) may be illustrated by the following examples:

*Example (1).* The taxpayer, on the calendar year basis, sustains a net operating loss in 1951 which forms the basis for a net operating loss deduction of $10,000 for 1952. In 1952 it has $6,000 net abnormal income, all of which is attributable to 1951. Although there would be no increase in excess profits tax for 1951 if the $6,000 net abnormal income were included in gross income for that year, the $6,000 would offset the $10,000 net operating loss for 1951. Therefore, the net operating loss deduction for 1952 would be reduced to $4,000 and the excess profits tax for 1952 would be increased to the extent caused by such reduction of the net operating loss deduction. The tax for 1952 is whichever of the following is the lesser:

(i) The tax for 1952 computed without excluding any net abnormal income from gross income, or

(ii) The tax for 1952 computed after excluding from gross income the $6,000 net abnormal income attributable to 1951, plus the increase in the tax so computed which would result if, by reason of the $6,000 being included in gross income for 1951, the net operating loss deduction available in computing excess profits net income for 1952 were only $4,000 instead of $10,000.

The taxpayer had net income and adjusted excess profits net income for 1952 after giving effect to the net operating loss deduction of $10,000. For 1953 it has $8,000 net abnormal income, all of which is attributable to 1951. The tax for 1953 is whichever of the following is the lesser:

(A) The tax for 1953 computed without excluding any net abnormal income from gross income; or

(B) The tax for 1953 computed after excluding from gross income the $8,000 net abnormal income attributable to 1951, plus the increase in the tax for 1951 and 1952 which would be caused by the reduction in the net operating loss for 1951 if the $8,000 were included in gross income for 1951 so that it offset the net operating loss sustained in that year. In making these computations for 1951 and 1952, the adjustments made for those years in applying section 456 (c) to 1952 are retained, that is, the $6,000 net abnormal income attributable to 1951 from 1952 in applying section 456 to 1952 is treated as if it remained in gross income for 1951, and the $6,000 net abnormal income attributable to 1951 from 1952 is not included in the gross income for 1952 and the net operating loss deduction for that year (prior to any adjustment caused by applying section 456 (c) to 1953) is treated as being $4,000, not $10,000.

*Example (2).* The taxpayer, on the calendar year basis, has $30,000 net abnormal income in 1950 attributable in the amount of $10,000 to each of the years 1951 to 1953. This $10,000 amount is therefore included in gross income for each of these years. In 1953 it has $60,000 net abnormal income, all of which is attributable to 1951. The tax for 1953 is whichever of the following is the lesser:

(i) The tax for 1953 computed under section 456 (d) without excluding any net abnormal income for 1953 from gross income; or

(ii) The tax for 1953 computed under section 456 (d) after excluding the $60,000 net abnormal income for 1953 from gross income, plus the increase in the tax for 1953 as so computed, if any, and the increase in tax, if any, for all previous taxable years which would result if the $60,000 net abnormal income were included in gross income for 1951.

(d) For any taxable year for which the excess profits tax or the increase in excess profits tax is determined under section 456 (c), excess profits net income, for purposes of section 430 (a) (2), shall include any amounts of items of net abnormal income attributable to such year under the provisions of section 456.

§ 40.456–5 *Computation of tax for future taxable years.* (a) Amounts of items of net abnormal income attributable to a future taxable year shall be included in the gross income for such future taxable year for the purposes of the excess profits tax, except that if in the application of section 456 (d) (1) to any future taxable year it is determined that the decrease in tax computed under section 456 (d) (1) (B) for the taxable year in which the net abnormal income was realized does not exceed the aggregate of the increases in tax for other taxable years with respect to such net abnormal income, as computed under section 456 (d) (1) (B), then no portion of such net abnormal income shall be included in gross income for any taxable year subsequent to such future taxable year. For example, in 1950 the taxpayer, on the calendar year basis, has $30,000 net abnormal income, of which $10,000 is attributable to each of the years 1951 to 1953. In applying section 456 (d) to 1952, it is determined that the decrease in tax for 1950 caused by the application of section 456 (c) (computed with the exclusion of the net abnormal income from gross income) does not exceed the increase in tax for 1951 caused by the inclusion in gross income of the net abnormal income attributable to that year. Therefore, the net abnormal income for 1950 attributable to 1953 shall not be included in gross income for that year.

(b) For the purpose of applying section 430 (a) (2) to a future taxable year in the income of which amounts of items of net abnormal income are includible under section 456, excess profits net income for such future taxable year shall include such amounts of items of net abnormal income so includible.

(c) If net abnormal income is included in the gross income for any future taxable year, and if the tax for such year is the amount determined under the limitations of section 456 (d) (1) with respect to such net abnormal income, then for the purpose of computing the net operating loss deduction or unused excess profits credit adjustment for any taxable year subsequent to such future taxable year the gross income for the future taxable year shall be deemed to include only such portion of the net abnormal income as, when added to the other gross income for such future taxable year, would result without the application of section 456 (d) (1) in an excess profits tax equal to the amount determined under that section.

(d) Section 456 (d) (1) provides that the excess profits tax for a future taxable year in which any portion of the net income for a previous taxable year is attributed is the smaller of the amounts determined under subparagraphs (1) and (2) of this paragraph:

(1) The excess profits tax for such year computed with the inclusion in gross income of such portion of the net abnormal income;

(2) The sum of—

(i) The excess profits tax for such year computed without the inclusion in gross income of such portion of the net abnormal income, and

(ii) The excess of—

(*a*) The decrease in excess profits tax for the year of realization which resulted from the exclusion of net abnormal income from the gross income for such year, over

(*b*) The aggregate of the increase in excess profits tax for the future taxable year (as determined under subdivision (i) of this subparagraph) and for intervening years resulting from the inclusion in the gross income for such intervening years of the other portions of such net abnormal income.

(e) If net abnormal income from more than one previous taxable year is attributed to the future taxable year, the determinations under paragraph (d) (1) and (2) of this section are to be made first with respect to the portion of net abnormal income attributed from the earliest previous taxable year, the portions of net abnormal income from the later taxable years being treated as

ordinary income for such future taxable year. The determinations under paragraph (d) (1) and (2) of this section are then to be made with respect to the portion of net abnormal income attributed from the next earliest previous taxable year, and for such purpose the excess profits tax for the future taxable year determined under paragraph (d) (1) of this section is considered the excess profits tax resulting from the determinations under paragraph (d) (1) and (2) of this section with respect to the net abnormal income attributed from the earliest previous taxable year, and the gross income referred to in paragraph (d) (2) of this section is considered that amount which would result in the tax reported under paragraph (d) (1) of this section if section 456 (d) (1) did not apply. The determinations for the other previous taxable years from which net abnormal income is attributed to the future taxable year are to be made in a similar manner in the order of such taxable years, and the amount so determined for the latest of such taxable years is the tax under section 456 (d) (1) for the future taxable year.

(f) If part of the income for a future taxable year, to which year net abnormal income of previous years is attributed, constitutes net abnormal income for such future year which is attributable to other taxable years, then the computations under section 456 (d) (1) shall be made without regard to the provisions of section 456 (c) which apply in determining the tax for such future taxable year. Section 456 (c) is applied after the tax is determined under the limitations of section 456 (d). In determining for the purpose of section 456 (d) (1) the increases and decreases in tax for previous taxable years, portions of net abnormal income for any of such previous taxable years attributable under section 456 (c) to other of such previous taxable years shall be treated as remaining in gross income in the years to which attributed.

§ 40.456–6 *Income arising out of a claim, award, judgment, or decree, or interest thereon.* (a) The first class of potentially abnormal income specifically set forth in section 456 (a) (2) is income arising out of a claim, award, judgment, or decree, or interest thereon. All items of such income are of the same class. Therefore, in determining whether income arising out of a judgment, for example, is abnormal either in kind or in amount, account must be taken not only of other judgment income, if any, received in preceding taxable years, but also of any income arising out of claims, awards, and decrees, and interest thereon, so received.

(b) In determining the portions of income of the class described which are attributable to other taxable years, due regard shall be given to the nature of the claim upon which the recovery is founded. Allocation will generally be made to the year or years during which occurred the exploitation, removal, or use, as the case may be, of the property right forming the subject matter of the claim, award, judgment, or decree. Thus, in the case of a judgment for infringement of a patent, the number of units produced through the use by the infringer of such patent in the respective years involved shall constitute a proper basis of allocation. Similarly, if the removal of minerals forms the basis of the recovery, the units removed in the respective years shall constitute a proper basis of allocation. The income arising from awards of a war claims commission, to the extent they constitute compensation for past losses, shall be attributed to the years during which such losses occurred. Interest shall be attributed to the years for which it was allowed.

(c) Example: (1) Based upon encroachment by the Y Corporation upon mineral property, the X Corporation in 1952 obtains judgment for and payment of $350,000. The X Corporation has not in any prior year derived income from any like source; nor are there any expenses involved in obtaining the judgment which are deductible for 1952. This amount, therefore, represents the net abnormal income, and is the only item included therein. As the judgment is based upon $1 per ton for ore removed in each year, the amount received is allocated as follows:

| Year | Tonnage | Income attributed |
|---|---|---|
| 1951 | 150,000 | $150,000 |
| 1952 | 200,000 | 200,000 |
| Total | | 350,000 |

There was no net operating loss deduction or unused excess profits credit adjustment in 1951 or 1952. For the purposes of the computation of the excess profits tax there shall be included in gross income for the year 1952 the amount of $200,000. The amount of $150,000 allocated to 1951 affects the total 1952 excess profits tax as explained below.

(2) The excess profits tax for the year 1952 shall be determined as follows:

(i) An excess profits tax for 1952 shall be computed without regard to section 456, that is, by including in gross income the item of $350,000, and

(ii) A partial excess profits tax for 1952 shall be computed on the net income arrived at by including in gross income only $200,000 of the item of $350,000, and to the partial tax so computed there shall be added the increase in the excess profits tax which would result from the inclusion in gross income for the year 1951 of $150,000 of the item of $350,000.

The excess profits tax for 1952 is either (i) or (ii), whichever is the lesser.

(3) To arrive at the increase in the excess profits taxes for 1951 which would result from the inclusion in the gross income for such year of $150,000 of the item of $350,000, the excess profits tax shall (but only for the purpose of determining the 1952 excess profits tax liability) be computed first by including the item of $150,000 in the gross income, and second by excluding such amount from the gross income. The excess of the amount obtained as the result of the first computation over the amount obtained as the result of the second computation represents such increase.

(4) If in the above example, in addition to the principal amount, interest had been added to the judgment, such interest would be also properly allocable as between 1952 and 1951 in accordance with the method sanctioned by the court in settling the amount of such interest. If the portion of the total interest attributable to the respective years cannot be ascertained from the judgment, such interest may be allocated among such years, upon the basis of the respective portions of the principal amount attributable to such years, giving effect to the period of time each portion remained unpaid.

§ 40.456–7 *Exploration, discovery, prospecting.* The second class of potentially abnormal income specifically set forth in section 456 (a) (2) is income resulting from exploration, discovery, or prospecting, or any combination thereof, extending over a period of more than 12 months. The exploration, discovery, or prospecting, must be that of the taxpayer. Income resulting from activities of such a character carried on by a predecessor is not entitled to the treatment provided in section 456, except as otherwise provided in section 462 (m).

§ 40.456–8 *Sale of patents, formulas or processes.* The third class of potentially abnormal income specifically set forth in section 456 (a) (2) is income resulting from the sale of patents, formulas, or processes or any combination thereof. The class also includes income resulting from the disposition of such property in an exchange upon which gain is recognized for the purpose of chapter 1.

§ 40.456–9 *Change in method of accounting.* The fourth class of potentially abnormal income specifically set forth in section 456 (a) (2) is income which is includible in gross income for the taxable year rather than for a different taxable year by reason of a change in the taxpayer's method of accounting. This class may include such items of income as are includible in gross income for the taxable year by reason of a change from the installment method to the straight accrual method of accounting, a change in inventory method, or a change from the reserve method to the specific charge-off method for the treatment of bad debts. Items of net abnormal income includible in gross income for the taxable year rather than for a different taxable year by reason of a change from the installment method to the straight accrual method of accounting shall be attributed to the year or years such items accrued. The method of allocating items of net abnormal income includible in gross income for the taxable year rather than for a different year by reason of other changes in accounting method is to be determined in each particular case upon consideration of all the facts in the case. See § 40.456–3 as to the statement required to be filed where the benefits of section 456 are claimed.

SEC. 457. CORPORATIONS COMPLETING CONTRACTS UNDER MERCHANT MARINE ACT.

(a) If the Federal Maritime Board certifies to the Secretary that the taxpayer has completed within the taxable year any contracts or subcontracts which are subject to the provisions of section 505 (b) of the Merchant Marine Act of 1936, as amended, then the tax imposed by this subchapter for such taxable year shall be, in lieu of a tax computed under section 430, a tax computed under subsection (b) of this section, if, and only if, the tax computed under subsection (b) is less than the tax computed under section 430.

(b) The tax computed under this subsection shall be the excess of—

(1) A tentative tax computed under section 430 with the normal-tax net income increased by the amount of any payments made, or to be made, to the Federal Maritime Board with respect to such contracts or subcontracts; over

(2) The amount of such payments.

§ 40.457–1 *Corporations completing contracts under Merchant Marine Act of 1936.* (a) Section 457 provides for an alternative tax in the case of a corporation which has been certified by the Federal Maritime Board (hereinafter referred to as the Board) to the Commissioner as having completed within the taxable year any contracts or subcontracts subject to the provisions of section 505 (b) of the Merchant Marine Act of 1936, as amended (hereinafter referred to as section 505 (b)). Under section 505 (b) a contractor or subcontractor is required to pay to the Board the amount of profit, if any, in excess of 10 percent of the total contract prices of such contracts or subcontracts.

(b) The alternative tax is in lieu of the excess profits tax computed under section 430 but only if such alternative tax is less than the tax under such section. Such alternative tax is the excess of (1) a tentative tax computed under section 430 with the normal-tax net income (used in computing excess profits net income) increased by the amount of any payments made, or to be made, to the Board with respect to contracts or subcontracts the completion of which during the taxable year has been certified to the Commissioner by the Board, over (2) the amount of such payments. If the excess profits tax is computed for a taxable year of less than 12 months, the tentative tax shall be the excess profits tax for such taxable year computed under section 433 (a) (2) except that for such purpose the normal-tax net income used in computing excess profits net income shall be increased by the amount of any payments made, or to be made, to the Board with respect to contracts or subcontracts subject to the provisions of section 505 (b).

(c) For the purposes of section 457, a certificate by the Board that the vessel or portion thereof covered by the contract or subcontract has been delivered subject to the provisions of section 505 (b) during the taxable year shall be deemed to be the certificate required by such section.

(d) A corporation claiming the benefit of section 457 shall attach to its excess profits tax return (1) a certificate of the Board showing each contract or subcontract subject to the provisions of section 505 (b) which the corporation has completed within the taxable year and (2) a statement showing the amount of payments made or to be made to the Board with respect to such contracts and subcontracts. If the amount of the payments made, or to be made, to the Board with respect to such contracts or subcontracts has not been ascertained at the time of filing the excess profits tax return, the corporation may estimate the amount of such payments for the purposes of section 457. In such cases, the Commissioner may require a bond from the corporation as a condition precedent to the computation of the tax under that section. If such a bond is required, it shall be on the form prescribed by the Commissioner and in such sum as the Commissioner may prescribe, and it shall be conditioned upon the payment by the corporation of any amount of tax found due upon redetermination of the tax made necessary by the estimated amount under section 457 (b) (2) proving incorrect, and upon such further conditions as the Commissioner may require. The bond shall be executed by the corporation as principal and by sureties satisfactory to the Commissioner. (See also section 1126 of the Revenue Act of 1926, as amended, paragraph 63 of the Appendix to Regulations 111 (Part 29 of this chapter).)

(e) If the amount actually paid, or to be paid, to the Board under section 505 (b) differs from the amount used in determining the tax under section 457, the corporation shall immediately notify the Commissioner of the amount actually paid, or to be paid, with respect to the particular contract. The Commissioner will thereupon redetermine the amount of the excess profits tax under section 457, and the amount of tax, if any, found to be due upon such redetermination shall be paid by the corporation upon notice and demand from the collector. The amount of tax, if any, shown upon redetermination to have been overpaid shall be credited or refunded to the taxpayer in accordance with the provisions of section 322.

SEC. 458. HISTORICAL INVESTED CAPITAL.

(a) *Definition of historical invested capital.* For the purposes of this subchapter the historical invested capital for any taxable year shall be the average invested capital for such year, determined under subsection (b). (For computation of invested capital in case of foreign corporations and corporations entitled to the benefits of section 251, see section 436 (b).)

(b) *Average invested capital.* The average invested capital for any taxable year shall be the aggregate of the daily invested capital for each day of such taxable year, divided by the number of days in such taxable year.

(c) *Daily invested capital.* The daily invested capital for any day of the taxable year shall be the sum of the equity invested capital for such day plus 75 per centum of the daily borrowed capital for such day determined under section 439 (b).

(d) *Equity invested capital.* The equity invested capital for any day of any taxable year shall be determined as of the beginning of such day and shall be the sum of the following amounts, reduced as provided in subsection (e)—

(1) *Money paid in.* Money previously paid in for stock, or as paid-in surplus, or as a contribution to capital;

(2) *Property paid in.* Property (other than money) previously paid in (regardless of the time paid in) for stock, or as paid-in surplus, or as a contribution to capital. Such property shall be included in an amount equal to its basis (unadjusted) for determining loss upon sale or exchange. If the property was disposed of before such taxable year, such basis shall be determined under the law applicable to the year of disposition, but without regard to the value of the property as of March 1, 1913. If the property was disposed of before March 1, 1913, its basis shall be considered to be its fair market value at the time paid in. If the unadjusted basis of the property is a substituted basis, such basis shall be adjusted, with respect to the period before the property was paid in, by an amount equal to the adjustments proper under section 115 (l) for determining earnings and profits. For the purposes of this section the fair value of additions and betterments made by the lessee to the physical properties of a lessor railroad corporation which have become the property of the lessor corporation by rejection of its lease (and fair value being determined as of the date such additions and betterments became the property of the lessor) shall be considered as a contribution to capital; and where the value of such improvements cannot be accurately determined by the old records thereof, because lost, incomplete, or inaccurate, the value of such improvements determined by the Interstate Commerce Commission for rate-making purposes shall be used in lieu of such fair value.

(3) *Distributions in stock.* Distributions in stock—

(A) Made prior to such taxable year to the extent to which they are considered distributions of earnings and profits; and

(B) Previously made during such taxable year to the extent to which they are considered distributions of earnings and profits other than earnings and profits of such taxable year;

(4) *Earnings and profits at beginning of year.* The accumulated earnings and profits as of the beginning of such taxable year;

(5) *Deficit in earnings and profits of another corporation.* In the case of a transferee, as defined in subsection (f) (4), an amount, determined under such paragraph, equal to the portion of the deficit in earnings and profits of a transferor attributable to property received previously to such day.

(e) *Reduction in equity invested capital.* The amount by which the equity invested capital for any day shall be reduced as provided in subsection (d) shall be the sum of the following amounts—

(1) *Distributions in previous years.* Distributions made prior to such taxable year which were not out of accumulated earnings and profits;

(2) *Distributions during the year.* Distributions previously made during such taxable year which are not out of the earnings and profits of such taxable year;

(3) *Earnings and profits of another corporation.* The earnings and profits of another corporation which previously at any time were included in accumulated earnings and profits by reason of a transaction described in section 112 (b) to (e), both inclusive, or in the corresponding provision of a prior revenue law, or by reason of the transfer by such other corporation to the taxpayer of property the basis of which in the hands of the taxpayer is or was determined with reference to its basis in the hands of such other corporation, or would have been so determined if the property had been other than money; and

(4) *Deficit in earnings and profits transferred to another corporation.* In the case of a transferor, as defined in subsection (f) (4), an amount, determined under such paragraph, equal to the portion of the deficit in earnings and profits of the transferor attributable to property transferred previously to such day.

(f) *Rules for application of subsections (d) and (e)—(1) Distributions to shareholders.* The term "distribution" means a

distribution by a corporation to its shareholders, and the term "distribution in stock" means a distribution by a corporation in its stock or rights to acquire its stock. To the extent that a distribution in stock is not considered a distribution of earnings and profits it shall not be considered a distribution. A distribution in stock shall not be regarded as money or property paid in for stock, or as paid-in surplus, or as a contribution to capital.

(2) *Distributions in first sixty days of taxable year.* In the application of such subsections so much of the distributions (taken in the order of time) made during the first sixty days thereof as does not exceed the accumulated earnings and profits as of the beginning thereof (computed without regard to this paragraph) shall be considered to have been made on the last day of the preceding taxable year. This paragraph shall not apply with respect to distributions made during the first sixty days of the taxpayer's first taxable year under this subchapter.

(3) *Computation of earnings and profits of taxable year.* For the purposes of subsections (d) (3) (B) and (e) (2) in determining whether a distribution is out of the earnings and profits of any taxable year, such earnings and profits shall be computed as of the close of such taxable year without diminution by reason of any distribution made during such taxable year or by reason of the tax under this subchapter or chapter 1 for such year and the determination shall be made without regard to the amount of earnings and profits at the time the distribution was made.

(4) *Deficit in earnings and profits—Earnings and profits of transferor and transferee.* If a corporation (hereinafter called "transferor") transfers substantially all its property to another corporation formed to acquire such property (hereinafter called "transferee"), if—

(A) The sole consideration for the transfer of such property is the transfer to the transferor or its shareholders of all the stock of all classes (except qualifying shares) of the transferee. (In determining whether the transfer is solely for stock, the assumption by the transferee of a liability of the transferor or the fact that the property acquired is subject to a liability shall be disregarded);

(B) The basis of the property, in the hands of the transferee, for the purposes of this subsection, is determined by reference to the basis of the property in the hands of the transferor;

(C) The transferor is forthwith completely liquidated in pursuance of the plan under which the acquisition of the property is made; and

(D) Immediately after the liquidation the shareholders of the transferor own all such stock;

for the purposes of this subchapter, in computing the equity invested capital for any day after the date of the acquisition of the property, the earnings and profits or deficit in earnings and profits of the transferee and the transferor shall be computed as if, immediately before the beginning of the taxable year in which such transfer occurs, the transferee had been in existence and sustained a recognized loss, and the transferor had realized a recognized gain, equal to the portion of the deficit in earnings and profits of the transferor attributable to such property.

(g) For special rules affecting computation of property paid in for stock in connection with certain exchanges and liquidations, see part III.

(h) The reserves of an insurance company shall not be included in computing equity invested capital under this section but shall be treated as daily borrowed capital as provided in section 439.

§ 40.458–1 *Historical invested capital method of determining invested capital—* (a) *In general.* A taxpayer computing its excess profits credit upon the basis of invested capital may, if it elects as provided by section 437 (b) (1), compute its invested capital under the so-called "historical invested capital" method. See § 40.437–2 for rules regarding election under section 437 (b) (1) and its effect. A foreign corporation and a corporation entitled to the benefits of section 251 may not compute invested capital under the historical invested capital method. See section 434 (b) and section 436 (b).

(b) *Determination of historical invested capital.* (1) Section 458 (a) defines "historical invested capital" as the "average invested capital" determined under section 458 (b). The "average invested capital" for any taxable year is defined by section 458 (b) as the aggregate of the "daily invested capital" for each day of such taxable year divided by the number of days in such taxable year. The "daily invested capital" for any day of the taxable year is defined by section 458 (c) as the sum of the "equity invested capital" for such day determined under section 458 (d), plus 75 percent of the "daily borrowed capital" for such day determined under section 439 (b). The historical invested capital shall in no event be an amount which is less than zero.

(2) The daily invested capital for any day is the sum of the equity invested capital for such day, determined under section 458 (d)–(h) (whether such equity invested capital be a positive amount or a negative amount), and 75 percent of the daily borrowed capital for such day, determined under section 439 (b). The daily invested capital of a transferee upon an exchange, as defined in section 471 (a), for any day after such exchange shall be reduced by the amount of any excess computed under the provisions of section 471 (c). If the amount of the equity invested capital determined under section 458 (d)–(h) is a negative amount and is not offset by borrowed invested capital, or if the amount of the reduction under section 471 (c) in daily invested capital is larger than the amount of such daily invested capital computed without regard to such reduction, the daily invested capital will be a negative amount.

(3) If, during the taxable year, a corporation is not involved in a tax-free liquidation and neither receives new capital, whether paid in or borrowed, nor makes any distribution other than out of earnings and profits of the taxable year, nor retires indebtedness of the character includible in borrowed capital, its average invested capital for the taxable year is an amount equal to its daily invested capital for the first day of the taxable year.

(4) In cases where the changes in invested capital are not numerous during the taxable year, the determination of the average invested capital may generally be simplified by taking the invested capital as of the first day of the taxable year and adding thereto such portion of each addition made during the year as the number of days remaining in the taxable year after such addition bears to the total number of days in the taxable year, and subtracting such portion of each reduction of capital as the number of days after such reduction bears to the total number of days in the taxable year. A simple method for determining average invested capital is illustrated by the following example:

*Example.* The daily invested capital of the X Corporation, which files its income tax returns on the calendar year basis, is $500,000 on January 1, 1951. The only changes in invested capital during the taxable year 1951 are as follows:

(a) On April 1, 1951, money amounting to $100,000 is paid in for stock.

(b) On October 1, 1951, a capital distribution is made amounting to $200,000.

| | |
|---|---|
| Aggregate invested capital from Jan. 1 to Apr. 1, inclusive (91 days), $500,000 × 91 | $45,500,000.00 |
| Aggregate invested capital from Apr. 2 to Oct. 1, inclusive (183 days) ($500,000 plus $100,000) × 183 | 109,800,000.00 |
| Aggregate invested capital from Oct. 2 to Dec. 31, inclusive (91 days) ($600,000 minus $200,000) × 91 | 36,400,000.00 |
| Aggregate invested capital for 1951 | 191,700,000.00 |
| Average invested capital for 1951 ($191,700,000 divided by 365, number of days in taxable year) | 525,205.48 |

§ 40.458–2 *Determination of equity invested capital; money and property paid in.* The equity invested capital for any day is determined as of the beginning of such day. The basis or starting point is found in the amount of money and property previously paid in for stock, or as paid-in surplus, or as a contribution to capital. The terms "money paid in" and "property paid in" do not include amounts received as premiums by an insurance company subject to taxation under section 204. For the purpose of determining equity invested capital, the amount of any property paid in is the unadjusted basis to the taxpayer for determining loss upon a sale or exchange under the law applicable to the taxable year for which the invested capital is being computed. If the property was disposed of after February 28, 1913, and before such taxable year, such unadjusted basis shall be determined under the law applicable to the year of disposition, but without regard to the value of the property as of March 1, 1913; if the property was disposed of before March 1, 1913, its unadjusted basis shall be considered to be its fair market value at the time paid in.

(b) If the basis to the taxpayer is cost and stock was issued for the property, the cost is the fair market value of such stock at the time of its issuance. If the stock had no established market value at the time of the exchange, the fair market value of the assets of the company at that time should be determined and the liabilities deducted. The resulting net worth will be deemed to represent the total value of the outstanding stock. In determining net worth for the purpose of fixing the fair market value of the stock at the time of the exchange, the property paid in for such stock shall

be included in the assets at its fair market value at that time.

(c) If stock having no established market value is issued for intangible property, and it is necessary to determine the fair market value of such property, the following factors, among others, may be taken into consideration in determining such value: (1) The earnings attributable to such intangible assets while in the hands of the predecessor owner; and (2) any cash offers for the purchase of the business, including the intangible property, at or about the time of its acquisition. A corporation claiming a value for intangible property paid in for stock should file with its return a full statement of the facts relating to such valuation.

(d) If the property was acquired after December 31, 1920, by a corporation from a shareholder as paid-in surplus or from any person as a contribution to capital, then the basis shall be the same as it would be in the hands of the transferor if the transfer had not been made. (See section 113 (a) (8).) If so acquired prior to January 1, 1921, the basis is the fair market value of the property at the time it was paid in. Where the basis is the transferor's basis, those adjustments shall be made to such basis with respect to the period before the property was paid in as are proper under section 115 (l) for determining earnings and profits. Thus, if A paid into a corporation in 1930 as paid-in surplus certain improved real estate purchased by him in 1920 for $20,000, with respect to which depreciation was allowed for the period held by him in amounts aggregating $6,000 (the full amount allowable), A's basis of $20,000 shall be reduced by $6,000 for the purpose of computing the invested capital of the corporation.

(e) The fact that the money or property paid in has been lost, destroyed, or otherwise disposed of shall not reduce the invested capital, except as such facts are reflected in the earnings and profits as of the beginning of the taxable year.

(f) As to determination of amount of property paid in for stock in connection with certain exchanges, see section 471 (b). See section 472 for rules for the elimination of duplication in invested capital as between two or more corporations.

(g) The fair value of additions and betterments made by the lessee to the physical properties of a lessor railroad corporation which have become the property of the lessor corporation by rejection of its lease (such fair value being determined as of the date such additions and betterments became the property of the lessor) shall be considered as a contribution to capital; and where the value of such improvements cannot be accurately determined by the old records thereof, because lost, incomplete, or inaccurate, the value of such improvements determined by the Interstate Commerce Commission for rate-making purposes shall be used in lieu of such fair value.

§ 40.458–3 *Determination of equity invested capital; distributions in stock.* A distribution made prior to the taxable year by a corporation in its stock, or in rights to acquire its stock, to the extent to which it constitutes a distribution of earnings and profits of the corporation, constitutes an item of equity invested capital. Such a distribution made during the taxable year out of earnings and profits other than out of the earnings and profits of that year is also an item of equity invested capital. If a stock dividend is paid out of capital and not out of earnings and profits, or is of such a character as not to be subject to tax in the hands of a distributee because exempt as a stock dividend either by statute or otherwise, it is not deemed to constitute a distribution and does not reduce the earnings and profits account. See section 115 (h).

§ 40.458–4 *Determination of equity invested capital; accumulated earnings and profits*—(a) *In general.* (1) The term "accumulated earnings and profits" is not defined in the Internal Revenue Code. See, however, section 115 and the regulations prescribed thereunder as to the effect of certain transactions on earnings and profits, and § 40.458–5 as to the effect of the declaration and distribution of dividends. In general, the concept of "accumulated earnings and profits" for the purpose of the excess profits tax is the same as for the purpose of the income tax. In computing accumulated earnings and profits as of the beginning of the taxable year, a taxpayer keeping its books and making its income tax returns on the accrual basis shall subtract the income and excess profits taxes for the preceding taxable year. If there is a deficit in the accumulated earnings and profits as of the beginning of the taxable year, such deficit shall not be taken into account in determining invested capital, and in such cases the earnings and profits as of the beginning of the taxable year shall be considered as zero, but subsequent earnings and profits shall be applied against such deficit. Unrealized appreciation in value of property is not a factor in determining earnings and profits.

(2) If the earnings and profits of another corporation have been included in the earnings and profits of the taxpayer by virtue of a transaction of the character referred to in section 458 (e) (3), for the purpose of computing the equity invested capital of the taxpayer for each day after the day of such transaction there shall be included in the accumulated earnings and profits of the taxpayer as of the beginning of its taxable year in which such transaction occurred the proportionate part of any earnings and profits of the other corporation accumulated prior to the beginning of such taxable year and properly allocable to the taxpayer; and there shall be included in the current earnings and profits of the taxpayer for such taxable year the proportionate part of any earnings and profits of such other corporation accumulated after the beginning of such taxable year and properly allocable to the taxpayer. The amount so included in the earnings and profits of the taxpayer as of the beginning of its taxable year in which the transaction occurred or in its current earnings and profits for such year shall not exceed such proportionate part of the earnings and profits of such other corporation accumulated as of the day on which such transaction occurred.

(3) If the transaction which resulted in the transfer to the taxpayer of the earnings and profits of another corporation constitutes an intercorporate liquidation subject to the provisions of section 472, the rule of the subparagraph (2) of this paragraph shall apply only with respect to that portion of such earnings and profits attributable to the stock of such other corporation held by the taxpayer with a basis determined under section 472 to be a basis other than cost. Section 472 (d) (1) provides for the adjustment appropriate with respect to the earnings and profits of such other corporation taken over in the liquidation attributable to the stock of such other corporation held by the taxpayer with a basis determined to be a cost basis.

(b) *Current earnings and profits.* (1) Earnings and profits of any taxable year cannot be included in the computation of invested capital for that year. If a dividend is declared and paid during any year out of the earnings and profits of that year and the stockholders pay back into the corporation all or a substantial part of the amount of such dividends, the amount so paid back cannot be included in the computation of invested capital for that year unless the corporation shows by evidence satisfactory to the Commissioner that the dividends were paid in good faith and without any understanding, express or implied, that they were to be paid back.

(2) In any case in which the earnings and profits of another corporation are included in the accumulated earnings and profits of the taxpayer by reason of a transaction of the character referred to in section 458 (e) (3), the proportionate part of any such earnings and profits accumulated after the beginning of the taxable year of the taxpayer in which such transaction occurred and allocable to the taxpayer, but in an amount not to exceed the proportionate part of the earnings and profits of such other corporation accumulated as of the day of such transaction, shall be considered to be current earnings of the taxpayer for such taxable year.

(3) The earnings and profits for the taxable year in which an intercorporate liquidation has occurred subject to the provisions of section 472 shall be increased or decreased, as the case may be, by the plus adjustment or the minus adjustment computed under section 472 (b) with respect to the stock of the liquidated corporation held by the taxpayer with a basis determined under section 472 to be a cost basis. See section 472 (d) (1).

§ 40.458–5 *Determination of equity invested capital; reductions by distributions.* (a) The amount of the equity invested capital for any day as partially determined by taking the aggregate of the sums described in section 458 (d) shall be reduced by the amount of the distributions made in prior taxable years which were not out of accumulated earnings and profits plus the amount of the distributions previously made during the taxable year which

were not out of the earnings or profits of such year. In determining whether a distribution is out of the earnings and profits of any taxable year, such earnings and profits shall be computed as of the close of such taxable year without diminution by reason of any distribution made during such taxable year or by reason of any income or excess profits tax imposed for such taxable year and without regard to the amount of earnings and profits at the time the distribution was made.

(b) For example, if a corporation making a return on the calendar year basis had accumulated earnings and profits as of the beginning of the taxable year of $50,000, and earnings and profits during the taxable year (without diminution by any distributions or by any income or excess profits tax for the taxable year) of $150,000, all earned during the last six months of the taxable year, and distributed $175,000 as dividends during the taxable year, $56,000 on April 1, $70,000 on July 1, and $49,000 on October 1, six-sevenths of each distribution will be deemed to have been paid out of earnings of the taxable year and one-seventh from accumulated earnings and profits, so that accumulated earnings and profits will be reduced by $8,000 beginning April 2, by an additional $10,000 beginning July 2, and by an additional $7,000 beginning October 2.

(c) In computing accumulated earnings and profits as of the beginning of the taxable year and in determining what distributions during the taxable year are made out of the earnings and profits of such year, for the purpose of section 458 (d) and (e), distributions made during the first 60 days of any taxable year, other than the taxpayer's first taxable year ending after June 30, 1950, are deemed, to the extent they do not exceed the accumulated earnings and profits as of the beginning of the taxable year, to have been made on the last day of the preceding taxable year. In applying such rule, such distributions shall be considered in the order of time. For example, if a corporation on the calendar year basis has accumulated earnings or profits of $100,000 on January 1, 1952, and makes distributions of $75,000 on January 15, 1952, and $50,000 on February 15, 1952, the distribution of January 15, 1952, and $25,000 of the distribution of February 15, 1952, are considered as having been made on December 31, 1951.

(d) A distribution is considered to be made on the date it is payable, except that where no date is set for its payment, the distribution is considered to be made on the date when it is declared, and except that distributions payable during the first 60 days of any taxable year, other than the taxpayer's first taxable year ending after June 30, 1950, are considered to be distributions made on the last day of the preceding taxable year to the extent such distributions do not exceed the accumulated earnings and profits as of the beginning of the taxable year.

(e) The purchase by a corporation of its own stock for investment does not of itself result in a reduction of equity invested capital. But see § 40.440–1 relative to inadmissible assets. If, however, the corporation subsequently cancels such stock, equity invested capital is reduced, beginning with the day following such cancellation, by so much of the adjusted basis of such stock in the hands of the corporation as is not properly chargeable to earnings and profits of the taxable year. If stock is purchased for retirement, there is a distribution on the date of purchase of the amount paid therefor and the equity invested capital is reduced by the amount thereof not properly chargeable to earnings and profits of the taxable year.

(f) The amount of distributions by a corporation whether in bonds of such corporation, or in money or other property may exceed the amount of the equity invested capital computed without regard to such distributions. In such event, the equity invested capital of such corporation for such day shall be reduced by virtue of such distributions to a negative amount.

§ 40.458–6 *Determination of equity invested capital, reduction by earnings and profits of another corporation.* (a) Section 458 (e) (3) provides for the elimination of the duplication which occurs in the computation of the equity invested capital of the taxpayer following a transaction of the character referred to therein, as a result of which the earnings and profits of another corporation became the earnings and profits of the taxpayer.[1] The earnings and profits of such other corporation having been included at the time of the transaction in the earnings and profits of the taxpayer, they remain continuously thereafter a part of such earnings and profits account for the purpose of computing for any day after such transaction the earnings and profits, the accumulated earnings and profits at the beginning of the taxable year, and the earnings and profits of the taxable year. In addition, however, the amount of such included earnings and profits is also brought into computation of equity invested capital of the taxpayer under provisions of section 458 other than section 458 (d) (4) relating to accumulated earnings and profits as of the beginning of the taxable year. Thus, if the transaction is a reorganization to which section 113 (a) (7) is applicable, and in which the taxpayer receives all the assets of another corporation in exchange solely for its own stock, such amount has already been taken into account in property paid in for stock under section 458 (d) (2); or if the transaction is an intercorporate liquidation of another corporation involving a distribution with respect to stock of such other corporation held by the taxpayer with a basis determined under section 472 to be a basis other than cost, such amount has already been taken into account in the computation of equity invested capital of the taxpayer, as adjusted under section 472 (d) (2).

(b) To preclude this duplicate inclusion of the earnings and profits of another corporation in the invested capital of the taxpayer, section 458 (e) (3) provides, as a step in the computation of equity invested capital, for the reduction of equity invested capital otherwise computed by the amount of earnings and profits of another corporation previously at any time included in the earnings and profits of the taxpayer. This adjustment is to be made in the computation of equity invested capital for each day after the day of such transaction, regardless of whether the earnings and profits absorbed were produced during the taxable year of the taxpayer in which such transaction occurred or in a prior taxable year, and regardless of the condition of the earnings and profits account of the taxpayer immediately prior to or at any time subsequent to the date of such transaction.

§ 40.458–7 *Determination of equity invested capital; deficit in earnings and profits of transferor transferred to transferee.* (a) The determination of the amount of money or property paid in for stock or as paid-in surplus or as a contribution to capital of the transferee on account of certain tax-free exchanges is prescribed by section 471. Such amount of property paid in is computed with respect to the unadjusted basis for determining loss of the property in the hands of the transferee, adjusted for the period prior to the time the property was paid in by amounts equal to the adjustments proper under section 115 (l) for determining earnings and profits, minus, inter alia, any liability of the transferor assumed upon the exchange or to which the property received was subject. Since the unadjusted basis of the property received minus any liabilities assumed by the transferee or to which the property received was subject, will reflect the amount of any deficit incurred by the transferor, the equity invested capital of the transferee resulting from the exchange would be reduced by the amount of such deficit, although the amount of such deficit would not have reduced the equity invested capital of the transferor, prior to the exchange, below the amount of its accumulated earnings and profits.

(b) (1) In certain cases where, despite a reorganization of the transferor involving a tax-free exchange of its assets, the corporate identity of the transferor is preserved, section 458 (d) (5) provides that equity invested capital of the transferee shall be increased by that portion of the deficit in earnings and profits of the transferor attributable to the property transferred by the transferor to the transferee. Section 458 (e) (4) provides for the complementary reduction in the equity invested capital of the transferor for any day after such a transfer by the amount of the deficit in earnings and profits attributable to the property transferred.

(2) If the transferee has received substantially all, but not all, the property of the transferor upon the exchange, the deficit in earnings and profits of the transferor attributable to the property transferred shall be an amount which bears the same ratio to the total deficit in earnings and profits of the transferor as the excess of the basis of

[1] Commissioner v. Sansome, 60 Fed. (2d) 931.

the property transferred to the transferee (adjusted by amounts equal to the adjustments proper under section 115 (l) for determining earnings and profits) over the amount of any liability of the transferor assumed upon the exchange and of any liability subject to which such property was so received bears to the excess of the basis of the total assets of the transferor immediately prior to the exchange (adjusted by amounts equal to the adjustments proper under section 115 (l) for determining earnings and profits) over the amount of any liability of the transferor, and the amount of any liability subject to which such assets were held immediately prior to the transfer.

(3) The adjustments provided by section 458 (d) (5) and section 458 (e) (4) are applicable only in case a corporation (called the transferor) transfers substantially all its property to another corporation formed especially to acquire such property (called the transferee), provided that—

(i) The sole consideration for the transfer of such property is the transfer to the transferor or its shareholders of all the stock of all classes (except qualifying shares) of the transferee. In determining whether the transfer is solely for stock, the assumption by the transferee of a liability of the transferor or the fact that the property acquired was received subject to a liability shall be disregarded;

(ii) The basis of the property in the hands of the transferee is determined by reference to the basis of such property in the hands of the transferor;

(iii) The transferor is forthwith completely liquidated in pursuance of the plan under which the acquisition of the property was made; and

(iv) Immediately after such liquidation the shareholders of the transferor own all the stock of the transferee received by the transferor.

(4) The earnings and profits of the transferee for any day after the date of acquisition of the property shall be considered to have been reduced by an amount equal to the amount by which the equity invested capital was increased pursuant to section 458 (d) (5), as if immediately before the beginning of the taxable year in which such transfer occurred the transferee had been in existence and had sustained a recognized loss equal to the portion of the deficit in earnings and profits of the transferor attributable to the property acquired by the transferee. The deficit in earnings and profits of the transferor for any day after the date of transfer of the property, and prior to the liquidation, must be decreased by the amount by which the equity invested capital is decreased pursuant to section 458 (e) (4), as if immediately before the beginning of the taxable year in which the transfer occurred the transferor had realized a recognized gain equal to the portion of the deficit in earnings and profits of the transferor attributable to the property transferred to the transferee.

(5) The provisions of section 458 (d) (5), section 458 (e) (4), and section 458 (f) (4) shall apply only in the case of a tax-free exchange involving a single transferor and shall not apply to instances where two or more transferors transfer property to a transferee in a tax-free exchange.

(6) The provisions of this section may be illustrated by the following example:

*Example.* In 1950 Corporation A, which was organized under the laws of the State of New York, found it necessary to incorporate under the laws of Delaware. Consequently a new Corporation B was organized under the laws of Delaware, and in exchange for all its stock received the entire assets of Corporation A. Immediately after the exchange Corporation A was liquidated, and the stock of Corporation B was transferred to the shareholders of Corporation A. Immediately prior to the exchange, the equity invested capital of Corporation A, consisting of money and property previously paid in for stock, was $500,000; in addition, Corporation A had a deficit in earnings and profits of $200,000. The adjusted basis of the assets of Corporation A at the time of the exchange properly adjusted under section 115 (l) for the computation of earnings and profits, and consequently the unadjusted basis of the assets to Corporation B at such time was $300,000. The equity invested capital of Corporation B., however, as of January 1, 1951, is $500,000, since section 458 (d) (5) requires the addition of Corporation A's $200,000 deficit to the equity invested capital of Corporation B, otherwise determined. As of January 1, 1951, Corporation B is also considered to have a deficit in earnings and profits of $200,000. If in 1951 Corporation B had earned $150,000, its equity invested capital as of January 1, 1952, would be $500,000 and its deficit in earnings and profits would be $50,000 ($200,000 minus $150,000). If in 1952 Corporation B had earned $75,000, its equity invested capital as of January 1, 1953, would be $525,000 ($500,000 plus $25,000 accumulated earnings and profits ($150,000 plus $75,000, minus $200,000)). Immediately after the exchange the equity invested capital of Corporation A would be $300,000 since section 458 (e) (4) requires the reduction of Corporation A's invested capital by the amount of any deficit in earnings and profits transferred to the transferee pursuant to the provisions of section 458 (f) (4), and Corporation A's deficit in earnings and profits computed pursuant to section 458 (f) (4) would be zero ($200,000 minus $200,000).

§ 40.458–8 *Determination of equity invested capital; insurance companies.* Section 458 (h) provides that the reserves of certain insurance companies shall not be included in computing equity invested capital but shall be treated as borrowed capital as provided in section 439. Section 458 does not apply to the computation of invested capital of mutual insurance companies other than life or marine. Such mutual insurance companies compute invested capital under section 437 (b) (3) only.

PART II—EXCESS PROFITS CREDIT BASED ON INCOME IN CONNECTION WITH CERTAIN EXCHANGES

SEC. 461. DEFINITIONS.

For the purposes of this part—

(a) *Acquiring corporation.* The term "acquiring corporation" means—

(1) A corporation which has acquired—

(A) Substantially all the properties of another corporation and the whole or a part of the consideration for the transfer of such properties is the transfer to such other corporation of all the stock of all classes (except qualifying shares) of the corporation which has acquired such properties, or

(B) Substantially all the properties of another corporation and the sole consideration for the transfer of such properties is the transfer to such other corporation of voting stock of the corporation which has acquired such properties, or

(C) Before December 1, 1950, properties of another corporation solely as paid-in surplus or a contribution to capital in respect of voting stock owned by such other corporation, or

(D) Substantially all the properties of a partnership in an exchange to which section 112 (b) (5), or so much of section 112 (c) or (e) as refers to section 112 (b) (5) is applicable.

(E) Properties either from one or more corporations or from one or more partnerships or from one or more corporations and one or more partnerships, other than from a corporation exempt under section 101, in an exchange, not otherwise described in this subsection, to which section 112 (b) (4) or (5), or so much of section 112 (c) or (e) as refers to section 112 (b) (4) or (5), is applicable.

For the purpose of subparagraphs (B) and (C) in determining whether such voting stock or such paid-in surplus or contribution to capital is the sole consideration, the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded. Subparagraph (C) shall apply only if the corporation transferring such properties is forthwith completely liquidated in pursuance of the plan under which the acquisition is made, and the transaction of which the acquisition is a part has the effect of a statutory merger or consolidation.

(2) A corporation which has acquired property from another corporation in a transaction with respect to which gain or loss was not recognized under section 112 (b) (6);

(3) A corporation the result of a statutory merger of two or more corporations; or

(4) A corporation the result of a statutory consolidation of two or more corporations.

(b) *Component corporation.* The term "component corporation" means—

(1) In the case of a transaction described in subsection (a) (1), the corporation which transferred the assets;

(2) In the case of a transaction described in subsection (a) (2), the corporation the property of which was acquired;

(3) In the case of a statutory merger, all corporations merged, except the corporation resulting from the merger; or

(4) In the case of a statutory consolidation, all corporation's consolidated, except the corporation resulting from the consolidation; or

(5) In the case of a transaction specified in subsection (a) (1) (D), the partnership whose properties were acquired.

(6) In the case of a transaction specified in subsection (a) (1) (E), the partnerships or corporations whose properties were required.

(c) *Income of certain component corporations not included.* For the purposes of section 434, section 462, section 463, and section 464, in the case of a corporation which is a component corporation in a transaction described in subsection (a)—

(1) Except as provided in paragraphs (2), (3), and (4), for the purpose of computing, for any taxable year ending after June 30, 1950, the excess profits credit of such component corporation or of an acquiring corporation of which the acquiring corporation in such transaction is not a component, no account shall be taken of the excess profits net income, or of the average base period net income if computed under section 442, 443, 444, 445, or 446, of such component corporation for any period before the day after such transaction, and no account shall be taken of capital additions in the base period computed under section 435 (f), and net capital additions or reductions computed under sec-

tion 435 (g), of such component corporation to the extent that such computations relate to any period before such transaction.

(2) Except as provided in paragraphs (3) and (4), in case such transaction occurred in a taxable year of such component corporation ending after June 30, 1950, for the purpose of computing the excess profits credit of such component corporation for such taxable year, the amount of its average base period net income shall be limited to an amount which bears the same ratio to such average base period net income (computed without regard to this paragraph) as the number of days in such taxable year before the day after such transaction bears to the total number of days in such taxable year.

(3) Except as provided in paragraph (4), in the case of a transaction described in subsection (a) (1) (E), for the purpose of computing the excess profits credit of such component corporation or of an acquiring corporation of which the acquiring corporation in such transaction is not a component, no account shall be taken of that portion of the excess profits net income, or of the average base period net income if computed under section 442, 443, 444, 445, or 446, of such component corporation, for any period before the day after such transaction which is allocable to the acquiring corporation in such transaction under section 462 (i), and no account shall be taken of that portion of capital additions in the base period computed under section 435 (f), and net capital additions or reductions computed under section 435 (g), of such component corporation, to the extent that such computations relate to any period before such transaction, which is allocable to the acquiring corporation in such transaction under section 462 (i);

(4) In the case of a transaction described in subsection (a) (1) (E) which occurred in a taxable year of such component corporation ending after June 30, 1950, for the purpose of computing the excess profits credit of such component corporation for such taxable year, the amount of its average base period net income shall be limited to the sum of the following:

(A) An amount which bears the same ratio to such average base period net income (computed without regard to this paragraph), as the number of days in such taxable year before the day after such transaction bears to the total number of days in such taxable year; and

(B) An amount which bears the same ratio to that portion of its average base period net income as is allocable to such component corporation in such transaction under section 462 (i) (computed without regard to this paragraph), as the number of days in such taxable year after the day of such transaction bears to the total number of days in such taxable year.

For the purposes of section 462, in the case of a corporation which is a component corporation in a transaction described in subsection (a), in computing for any taxable year the average base period net income of the acquiring corporation in such transaction, no account shall be taken of the excess profits net income, or of the average base period net income, of such component corporation for any period beginning with the day after such transaction.

(d) For purposes of sections 435 (e), 442, 443, 444, 445, and 446, any taxpayer which is an acquiring corporation shall be considered to have been in existence and to have had taxable years for any period during which it or any of its component corporations was in existence, and such corporation shall be considered to have commenced business on the earliest date on which it or any of its component corporations commenced business. Except for purposes of the previous sentence, a component corporation in a transaction described in subsection (a), other than one described in subsection (a) (1) (E), shall be deemed not to have been in existence or to have commenced business prior to the day after such transaction for purposes of determining the applicability of sections 435 (e), 442, 443, 444, 445, and 446, to such corporation after such transaction. For purposes of the first sentence of this subsection, a corporation which was an acquiring corporation in a previous transaction shall be deemed to have been in existence for such period as is determined by the application of that sentence to that corporation with respect to that transaction. For purposes of this part, where sections 443 (b), 444 (c), 445 (b), and 446 (b) refer to the amount of a taxpayer's total assets as of the last day of its taxable year immediately preceding the taxpayer's first taxable year under this subchapter, such references, where appropriate, shall be taken to mean the amount of such taxpayer's total assets as of the last day of its base period.

(e) *Component corporation which was an acquiring corporation in a previous transaction.* In the case of a component corporation which was an acquiring corporation in a previous transaction, its average base period net income, for purposes of the later transaction, shall be determined under sections 435 (d), 435 (e), or 442 (c) with the application of section 462 (b), and of section 462 (c) or (d), where applicable, with respect to the previous transaction, and its average base period net income, for purposes of the later transaction, shall be determined under sections 442 (d), 443, 444, 445, or 446, with the application of sections 462 (d), (e), (f), (g), or (h), where applicable with respect to the previous transaction.

(f) *Sole proprietorship.* For the purposes of sections 461 (a) (1) (D), 461 (b) (5), and 462 (k), a business owned by a sole proprietorship shall be considered a partnership.

SEC. 462. AVERAGE BASE PERIOD NET INCOME—DETERMINATION.

(a) *In general.* In the case of a taxpayer which is an acquiring corporation, for the purposes of the determination of its average base period net income under section 435 (c), its average base period net income determined under section 435 (d) may be determined by computing its excess profits net income either with or without reference to section 462 (b), and its average base period net income under sections 435 (e) or 442 (c), subject to the rules provided in section 462 (c) or (d), may likewise be determined by computing its excess profits net income either with or without reference to section 462 (b). Its average base period net income under sections 442 (d), 443, 444, 445, and 446 shall be determined subject to the rules provided in sections 462 (d), (e), (f), (g), and (h). The excess profits net income of such acquiring corporation, computed with reference to section 462 (b), shall be the excess profits net income for each month of the acquiring corporation's base period, and for the additional period ending June 30, 1950, increased or decreased, as the case may be, by the addition or reduction resulting from including the excess profits net income for that month of all component corporations in the manner provided in subsection (b).

(b) *Method of recomputation of excess profits net income of acquiring corporation.* (1) The excess profits net income for each month in the base period of the acquiring corporation and for each month in the additional period ending June 30, 1950, shall be determined in the case of the acquiring corporation, and of any component corporation, as provided in section 435 (d) (1) without regard, however, to that part of such section which provides that in no event shall the excess profits net income of any corporation for any month be less than zero.

(2) For the purposes of this section, if the acquiring corporation was in existence, as provided in section 461 (d), at the beginning of its base period and, for any full month of such base period, either the acquiring corporation or any component corporation was not in existence, such corporation's excess profits net income for such month shall, nothwithstanding the last sentence of section 435 (d) (1), be an amount equal to 1 per centum of the equity capital (as defined in section 437 (c)) of such corporation at the close of the day before the transaction described in section 461 (a) occurred, or at the close of the base period of such corporation, whichever is earlier, reduced by an amount determined under section 440 (b) (relating to ratio of inadmissible assets), by applying section 440 (b) as of the day before the transaction described in section 461 (a) occurred, or at the close of the base period of such corporation, whichever is earlier. In case either the acquiring corporation or any component corporation owned stock in any other such corporation on the first day of such owning corporation's first taxable year under this subchapter, the amounts computed under this paragraph with respect to such corporations shall be adjusted, under regulations prescribed by the Secretary, to such extent as may be necessary to prevent the excess profits net income of such corporations for the base period of the acquiring corporation from reflecting money or property having been paid in by either of such corporations to the other for stock or as paid-in surplus or as a contribution to capital, or from reflecting stock of either having been paid in for stock of the other or as paid-in surplus or as a contribution to capital. For the purposes of this paragraph, stock in either such corporation which has in the hands of the other corporation a basis determined with reference to the basis of stock previously acquired by the issuance of such other corporation's own stock shall be deemed to have been paid in for the stock of such other corporation.

(3) For every month of the acquiring corporation's base period and for each month thereafter for the period ending June 30, 1950, there shall be added to the excess profits net income of the acquiring corporation for that month, as determined under paragraphs (1) and (2), the excess profits net income of each component corporation for that month so determined. The excess profits net income of the acquiring corporation for any month, recomputed as provided in the previous sentence, shall, in no event, be less than zero.

(c) *Use by acquiring corporation of alternative average base period net income based on growth provided for in section 435 (e).* (1) In the case of a transaction described in section 461 (a), other than a transaction described in section 461 (a) (1) (E),

(A) Where, immediately prior to the date of the transaction, the acquiring corporation and all the component corporations (other than a corporation created incident to such transaction) had commenced business prior to the beginning of its base period (determined without reference to section 461 (d)) and met the requirements of section 453 (e) (1) (A) (i):

(i) The acquiring corporation shall not be denied the right to determine whether it is eligible for the benefits of section 435 (e) without reference to the recomputation of its excess profits net income provided for in section 462 (b) where the transaction occurred on or after July 1, 1950, but it shall be denied such right where the transaction occurred prior to July 1, 1950, and

(ii) The acquiring corporation shall be entitled to compute its average base period net income under section 435 (e) with reference to the recomputation of its excess profits net income provided for in section 462 (b) if the tests of section 435 (e) are satisfied. For that purpose, the acquiring corporation shall combine with its total payroll and its total gross receipts for that portion of its base

period which preceded such transaction the total payroll and total gross receipts of such component corporations for that portion of such period and it shall combine with its net sales for that portion of the period prior to January 1, 1951, which preceded such transactions the net sales of such component corporations for that portion of such period. The allocation of payroll and gross receipts amounts of a component corporation to any such portion of such period shall be made in accordance with the rules provided in section 435 (e) (4) and (5). For purposes of qualifying under section 435 (e) (1) (A) (i) (relating to total assets of the taxpayer), such acquiring corporation shall combine its total assets on the date specified in section 435 (e) (1) (A) (i) with the total assets of each component corporation on such date. The Secretary shall prescribe by regulation such rules as may be necessary to insure that such combined total gross receipts do not reflect a duplication for purposes of this section;

(B) Where, immediately prior to the date of the transaction, either the acquiring corporation or one or more component corporations, had commenced business prior to the beginning of its base period (determined without reference to section 461 (d)) and met the requirements of section 435 (e) (1) (A) (i), but where either the acquiring corporation or one or more of such component corporations (other than a corporation created incident to such transaction) did not meet such requirements, the acquiring corporation shall not be entitled to compute its average base period net income under section 435 (e), regardless of the date on which the transaction occurred, or of whether or not, after the transaction, it determines its excess profits net income with reference to the recomputation provided for in section 462 (b). In any such case, where the transaction occurred on or after July 1, 1950, the monthly excess profits net income of the corporation entitled to the benefits of section 435 (e) for any month of the acquiring corporation's base period shall be, for purposes of the recomputation provided for in section 462 (b), one-twelfth of the average base period net income to which such corporation was entitled under section 435 (e).

(2) In the case of a transaction described in section 461 (a) (1) (E) which occurred after the close of the base period of the component corporation in whcih the component corporation, immediately prior to the date of the transaction, was entitled to the use of the alternative average base period net income based on growth provided for in section 435 (e), the acquiring corporation, if it determines its excess profits net income with reference to the recomputation provided for in section 462 (b), and the component corporation shall be entitled to compute their average base period net incomes under section 435 (e). Where the transaction occurred during the base period of the acquiring corporation, and the component corporation, immediately prior to the date of the transaction, had commenced business prior to the beginning of its base period (determined without reference to section 461 (d)) and met the requirements of section 435 (e) (1) (A) (i), the acquiring corporation, if it determines its excess profits net income with reference to the recomputation provided for in section 462 (b), and the component corporation, shall be entitled to compute their average base period net incomes under section 435 (e) provided, however, that they meet the tests of that section. For that purpose, the payroll and gross receipts of the component corporation for the period prior to the day of the transaction, determined in accordance with the rules provided in section 435 (e) (4) and (5), and the net sales of the component corporation for the period prior to the date of the transaction, shall be allocated as between the component corporation and the acquiring corporation in the same ratio as the excess profits net income of the component corporation allocated under subsection (i), and such allocated payroll, gross receipts, and net sales amounts shall be treated by the component corporation and by the acquiring corporation as the payroll, gross receipts, and net sales of the component corporation and the acquiring corporation for the period prior to the transaction. In the application of the test prescribed in section 435 (e) (1) (A) (i) (relating to total assets of the taxpayer) the component corporation and the acquiring corporation shall each be considered as having held the total assets of the component corporation as of the date applicable for purposes of section 435 (e) (1) (A) (i).

(3) Where any corporation, a party to a transaction described in section 461 (a), which had commenced business prior to the beginning of its base period (determined without reference to section 461 (d)), either was entitled at the time of the transaction to determine its average base period net income under section 435 (e) by reason of its having met the requirements of section 435 (e) (1) (B) or, where the transaction occurred prior to January 1, 1951, was furnishing at the time of the transaction a product or class of products of the type described in section 435 (e) (1) (B) (ii), the acquiring corporation shall be entitled to determine its average base period net income under section 435 (e) as provided in this subsection, substituting, for purposes of this paragraph, for the reference to the requirements of section 435 (e) (1) (A) (i), wherever it appears in paragraphs (1) and (2), a reference to the requirements stated in this paragraph, for the date July 1, 1950, wherever it appears in paragraph (1), the date January 1, 1951, and for the references, as they appear in paragraph (2), to transactions which occurred after the close of the base period of the component corporation and to transactions which occurred during the base period of the acquiring corporation, references to transactions which occurred after December 31, 1950, and to transactions which occurred prior to January 1, 1951, respectively.

(d) *Use by acquiring corporation of alternative average base period net income provided in the case of base period abnormalities in section 442.* (1) In the case of a transaction described in section 461 (a) which occurred during the base period of an acquiring corporation which commenced business (as provided in section 461 (d)) prior to the beginning of its base period, the acquiring corporation shall be entitled to determine its average base period net income under section 442 (c) or (d) if it satisfies the requirements of either such subsection and satisfies the other requirements of section 442. For purposes of section 442—

(A) In the case of such a transaction, other than a transaction described in section 461 (a) (1) (E), for purposes:

(i) Of determining excess profits net income for any month of the base period for purposes of section 442 (c) or (d), such acquiring corporation shall recompute its monthly excess profits net income as provided in section 462 (b), but without regard to the last sentence of section 462 (b) (3);

(ii) Of the computation provided in section 442 (d) (1) or (e) (1) (A) with respect to any day, the acquiring corporation shall be considered as having had the total assets of its component corporation or corporations on such day;

(iii) Of the interest adjustment provided in section 442 (d) (4) and (e) (1) (B), the acquiring corporation shall be considered as having paid or incurred the interest paid or incurred by its component corporation or corporations for that part of such periods as is referred to in those sections as preceded the date of the transaction; and

(iv) Of determining the existence of an abnormality under section 442 (a) with respect to the period prior to such transaction, the acquiring corporation shall be treated as if the component corporation's business during such period were its own; and

(B) In the case of a transaction described in section 461 (a) (1) (E), for purposes:

(i) Of determining excess profits net income for any month of the base period for purposes of section 442 (c) or (d), such acquiring corporation shall be considered as having had for that month that proportion of the excess profits net income (or deficit in excess profits net income) of the component corporation for such month which is allocable to such acquiring corporation under section 462 (i);

(ii) Of the computation referred to in subparagraph (A) (ii) of this paragraph and of the interest adjustment referred to in subparagraph (A) (iii) of this paragraph, the acquiring corporation shall be considered as having had the same portion of the items referred to in those subparagraphs as the ratio of its allocable share of the excess profits net income of the component corporation under section 462 (i) bears to the total excess profits net income of that corporation; and

(iii) Of determining the existence of an abnormality under section 442 (a) with respect to the period prior to such transaction, the acquiring corporation shall be treated as if that portion of the component corporation's business which was subsequently transferred to the acquiring corporation had been its own.

(2) In the case of a transaction described in section 461 (a) which occurred after the close of the base period of an acquiring corporation which commenced business (as provided in section 461 (d)) prior to the beginning of its base period, the acquiring corporation shall not be entitled to determine its average base period net income under section 442 except that:

(A) If all of the corporations, parties to the transaction, were, prior to the transaction, entitled to compute their average base period net incomes under section 442 (d) or under sections 442 (d), 443, 444, 445, or 446, the acquiring corporation may add an average base period net income of any such corporation computed under section 442 (d) to such other average base period net incomes for the purpose of determining its average base period net income after the transaction under the section applicable to it prior to the transaction, and

(B) If all of the corporations, parties to the transaction, were, prior to the transaction, entitled to compute their average base period net incomes under section 442 (c), if some were so entitled under section 442 (c) and the remainder under section 442 (d), or if some, but not all, were so entitled under either section 442 (c) or (d), then, for purposes of the recomputation of the excess profits net income of the acquiring corporation under section 462 (b), and for purposes of the allocation of a portion of the excess profits net income (or deficit in excess profits net income) of the component corporation to the acquiring corporation under section 462 (i) in the case of a transaction described in section 461 (a) (1) (E).

(i) In the case of an average base period net income computed under section 442 (c), the substitute excess profits net income of the corporation for any month determined under section 442 (c) (1) shall be treated as the excess profits net income of that corporation for that month; and

(ii) In the case of an average base period net income computed under section 442 (d), a figure obtained by dividing such average base period net income by 12 shall be treated as the excess profits net income of that corporation for any month of its base period.

(3) In the case of a transaction described in section 461 (a), where the acquiring corporation had not commenced business, within the meaning of section 461 (d), prior to the beginning of its base period, the acquiring corporation shall not be entitled to compute its average base period net income under section 442 in the manner provided therein or as provided in this section.

(e) *Use by acquiring corporation of alternative average base period net income provided for change in products or services in section 443.* (1) In the case of a transaction described in section 461 (a), other than a transaction described in 461 (a) (1) (E), where the acquiring corporation had commenced business, within the meaning of section 461 (d), on or before the first day of its base period, the following rules shall be applicable in determining the availability to the acquiring corporation of a right to compute its average base period net income under section 443—

(A) Except as provided in subparagraphs (B) and (D), where any corporation a party to the transaction, other than a corporation created incident to such transaction, had not commenced business, without regard to section 461 (d), on or before the first day of the acquiring corporation's base period, the acquiring corporation shall not be entitled to compute its average base period net income under section 443.

(B) In a case described in subparagraph (A) above, where the acquiring corporation, other than a corporation created incident to such transaction, and all of the component corporations were, prior to the transaction, entitled to compute their average base period net incomes under sections 442 (d), 443, 444, 445 or 446, the acquiring corporation may add an average base period net income computed under section 443 of any of the parties to the transaction to such other average base period net incomes for the purpose of determining its average base period net income after the transaction under the section applicable to it prior to the transaction.

(C) Where, at the time of the transaction, one or more of the corporations, parties to the transaction, had made a substantial change, within the meaning of section 443 (a) (1), in the products or services which it furnished, but where such corporations were not entitled at such time to compute their average base period net incomes under section 443, the acquiring corporation, if it recomputes its excess profits net income in the manner provided in section 462 (b) (but without regard to the last sentence of section 462 (b) (3)), shall be entitled to compute its average base period net income under section 443 if the requirements of that section are satisfied. For that purpose the gross income of all of the component corporations for taxable years beginning with, within, and subsequent to, the taxable year of the corporation which made the first such change in which such change was made shall be treated as having been earned by the acquiring corporation. The total assets of the component corporations as they existed on the last day of such year of the acquiring corporation which preceded the taxable year in which the transaction occurred shall be treated, for purposes of the determination of its average base period net income under section 443 for the taxable year of the transaction and for subsequent taxable years, as having been held by the acquiring corporation on such day. Interest paid or incurred by any component corporation prior to the day of the transaction shall be considered as having been paid or incurred by the acquired corporation at the time when it was paid or incurred by such component corporation. In any such case, each such change shall be treated as having been made by the acquiring corporation at the time when it was made by the corporation making the change.

(D) In the case described in subparagraph (A), where a corporation a party to the transaction commenced business during the 36-month period ending on the last day of the base period of the acquiring corporation, and the transaction occurred prior to December 1, 1950, the activities of that corporation shall be treated for purposes of section 443, and with respect to the activities of the other corporations parties to the transaction, as though they constituted a substantial change in products or services furnished, within the meaning of section 443 (a) (1), by the acquiring corporation and, for purposes of determining whether or not the acquiring corporation meets the requirements of that section, the rules prescribed in subparagraph (C) shall be applicable.

(E) Where there was a substantial change in the products or services furnished by the acquiring corporation subsequent to the date of the transaction, the acquiring corporation shall be entitled to determine its average base period net income under section 443 with respect to such change if it recomputes its excess profits net income in the manner provided in section 462 (b) (without regard to the last sentence of section 462 (b) (3)), subject to the application of the rules prescribed in subparagraph (C).

(F) Subject to the application of the above rules, an acquiring corporation shall not be deemed, for purposes of section 443, to have made a substantial change in the products or services furnished by it solely by reason of a change in such products or services resulting from the execution of a transaction described in section 461 (a).

(2) In the case of a transaction described in section 461 (a) (1) (E), the acquiring corporation shall only be entitled to compute its average base period net income under section 443 where:

(A) The component corporation was entitled to compute its average base period net income under section 443 prior to the date of the transaction, in which event such average base period net income shall be allocated as between the acquiring corporation and the component corporation in the manner provided in section 462 (i), or

(B) There was, after the date of the transaction, a substantial change in the products or services furnished by the acquiring corporation and the acquiring corporation determines its excess profits net income for each month of the base period by reference to the excess profits net income allocable to it in the manner provided in section 462 (i).

(3) In the case of a transaction described in section 461 (a), where the acquiring corporation had not commenced business, within the meaning of section 461 (d), on or before the first day of its base period, the acquiring corporations shall not be entitled to compute its average base period net income under section 443 in the manner provided therein or as provided in this section.

(f) *Use by acquiring corporation of alternative average base period net income provided in the case of increase in capacity for production or operation in section 444.* Where any corporation, a party to a transaction described in section 461 (a) which occurred after the close of the base period of the acquiring corporation, was entitled to compute its average base period net income under section 444, the acquiring corporation shall only be entitled to compute its average base period net income under such section where all of the corporations, parties to the transaction, (other than a corporation created incident to the transaction) were entitled to compute their average base period net incomes under sections 442 (d), 443, 444, 445 or 446, in which case the acquiring corporation may add an average base period net income computed under section 444, or an allocable portion thereof determined under section 462 (i), of any of the parties to the transaction to such other average base period net incomes for the purpose of determining its average base period net income after the transaction under the section applicable to it prior to the transaction. Where, in the case of a corporation entitled to compute its average base period net income under section 444, the transaction described in section 461 (a) occurred prior to the time at which any corporation a party to the transaction was entitled to compute its average base period net income under section 444, the Secretary, pursuant to regulations, shall provide for the extent to which and for the manner in which the acquiring corporation shall be entitled to compute its average base period net income under such section.

(g) *Use by acquiring corporation of alternative average base period net income provided for new corporations in section 445.* (1) In the case of a transaction described in section 461 (a) which occurred during the base period of the acquiring corporation, such acquiring corporation shall be entitled to compute its average base period net income under section 445, in the manner provided therein, if such corporation had not commenced business, within the meaning of section 461 (d), prior to the beginning of its base period and, in applying section 445, the number of taxable years since the acquiring corporation is deemed to have commenced business under section 461 (d) shall be determinative.

(2) In the case of a transaction described in section 461 (a) which occurred after the close of the base period of an acquiring corporation which had not commenced business, within the meaning of section 461 (d), prior to the beginning of its base period—

(A) Where such transaction is a transaction other than a transaction described in section 461 (a) (1) (E)—

(i) And the transaction occurred after the close of the third taxable year after the commencement of business of the component corporation or corporations and of the acquiring corporation (unless such corporation was created incident to the transaction), the commencement of business for each such corporation being determined without regard to section 461 (d), the average base period net income of the acquiring corporation after the transaction shall be determined, for purposes of section 445, in lieu of in the manner provided by section 445 (b), by adding together the average base period net incomes of the acquiring corporation and of the component corporation or corporations as determined under that section as of the first day of the fourth such taxable year of each such corporation;

(ii) And the transaction occurred prior to the close of the third taxable year after the commencement of business of either the acquiring corporation or of one or more of the component corporations, determined without regard to section 461 (d), but after the close of the third taxable year after the commencement of business of one or more of such corporations, the average base period net income of the acquiring corporation after the transaction shall be determined, for purposes of section 445, in lieu of in the manner provided by section 445 (b), by adding together the average base period net incomes determined under section 445 as of the first day of the fourth such taxable year of each such corporation in business for more than three taxable years and an average base period net income amount computed by the method specified in section 445 for each corporation not in business for three taxable years as though the day immediately prior to such transaction were the first day of such corporation's fourth such taxable year;

(iii) And the transaction occurred prior to the close of the third taxable year after the commencement of business of the acquiring corporation and of the component corporation or corporations, the average base period net income of the acquiring corporation after the transaction shall be determined, for purposes of section 445, by the method specified in section 445, and, in applying that

method, the number of taxable years since the acquiring corporation is deemed to have commenced business under section 461 (d) shall be determinative;

(B) Where such transaction is a transaction described in section 461 (a) (1) (E)—

(i) And the transaction occurred after the close of the third taxable year after the commencement of business of the component corporation, the average base period net income of the acquiring corporation after the transaction shall be that portion of the average base period net income of the component corporation, determined under section 445, which is allocable to the acquiring corporation under section 462 (i);

(ii) And the transaction occurred prior to the close of the third taxable year after the commencement of business of the component corporation, the average base period net income of the acquiring corporation after the transaction shall be determined, for purposes of section 445, by the method specified in section 445 and, in applying that method, the number of taxable years since the acquiring corporation is deemed to have commenced business under section 461 (d) shall be determinative.

(3) In the case of a transaction described in section 461 (a) where the acquiring corporation had commenced business, within the meaning of section 461 (d), prior to the beginning of its base period, the acquiring corporation shall not be entitled to compute its average base period net income under section 445 in the manner provided therein or as provided in this section. In any such case, however, where the acquiring corporation (other than a corporation created incident to the transaction) and all of the component corporations were, prior to the transaction, entitled to compute their average base period net incomes under sections 442 (d), 443, 444, 445, or 446, the acquiring corporation may add an average base period net income computed under section 445 of any of the parties to the transaction to such other average base period net incomes for the purpose of determining its average base period net income after the transaction under the section applicable to it prior to the transaction.

(h) *Use by acquiring corporation of alternative average base period net income provided for depressed industries in section 446.* Where any corporation, a party to a transaction described in section 461 (a) which occurred after the close of the base period of the acquiring corporation, was entitled to compute its average base period net income under section 446, the acquiring corporation shall only be entitled to compute its average base period net income under such section where all of the corporations, parties to the transaction (other than a corporation created incident to the transaction), were entitled to compute their average base period net incomes under sections 442 (d), 443, 444, 445, or 446, in which case the acquiring corporation may add an average base period net income computed under section 446, or an allocable portion thereof determined under section 462 (i), of any of the parties to the transaction to such other average base period net incomes for the purpose of determining its average base period net income after the transaction under the section applicable to it prior to the transaction. Where, in the case of a corporation entitled to compute its average base period net income under section 446, the transaction described in section 461 (a) occurred prior to the time at which any corporation a party to the transaction was entitled to compute its average base period net income under section 446, the Secretary, pursuant to regulations, shall provide for the extent to which and for the manner in which the acquiring corporation shall be entitled to compute its average base period net income under such section.

(i) *Allocation rules in the case of transactions described in section 461 (a) (1) (E).* (1) The amount of the component corporation's excess profits net income for any month which shall be taken into account by the acquiring corporation in the computation of its excess profits net income as provided in subsection (b) shall be such portion of the component corporation's excess profits net income, or of its substitute excess profits net income if computed under section 442 (c), for such month as the fair market value of the assets transferred to the acquiring corporation bears to the fair market value of the total assets of the component corporation as they existed immediately prior to such transaction.

(2) In the case of a transaction which occurred after the close of the third taxable year after a component corporation commenced business, the amount of its average base period net income, if computed under section 445 (relating to new corporations), for such taxable year and for any taxable year thereafter which is allocable to the acquiring corporation shall be such portion of the component corporation's average base period net income computed under such section as the fair market value of the assets transferred by the component corporation to the acquiring corporation bears to the fair market value of the total assets of the component corporation as they existed immediately prior to the transaction.

(3) For the purposes of section 461 (c) (4) (B), the average base period net income allocable to the component corporation, other than in the case of an average base period net income computed under section 445 (b) (1), shall be such portion of its average base period net income computed under section 435 (c) as the fair market value of the assets not transferred in the transaction bears to the fair market value of the assets held immediately prior to such transaction.

(4) In the case of a transaction which occurred after the requirements of sections 442 (d), 443, 444, or 446 are met by the component corporation, the amount of the component corporation's average base period net income, if computed under any of such sections, for such taxable year, which is allocable to the acquiring corporation, shall be such portion of the component corporation's average base period net income computed under such section as the fair market value of the assets transferred by the component corporation to the acquiring corporation bears to the fair market value of the total assets of the component corporation as they existed immediately prior to the transaction.

(5) Pursuant to regulations prescribed by the Secretary, a determination of the fair market value of the properties and of the division thereof for the purpose of this subsection, may be made by agreement between all persons parties to the transaction, where the Secretary consents thereto. In no such case shall the aggregate of the excess profits net incomes or of the average base period net incomes allocated under the above paragraphs be in excess of 100 per centum of the excess profits net income or of such average base period net income, as the case may be, of the component corporation.

(6) Pursuant to regulations prescribed by the Secretary, an allocation of excess profits net income or average base period net income for the purposes of this section may be made on the basis of the earnings experience of the assets transferred and retained in lieu of an allocation based on the fair market value of the assets if all of the parties to the transaction consent thereto and if it is established to the satisfaction of the Secretary that such an allocation fairly represents an identifiable earnings experience of each such group of assets. Except in the case of a transaction which occurred before December 1, 1950, in which the component corporation is a partnership, the aggregate of the excess profits net incomes or average base period net incomes allocated to the several parties to the transaction as provided in this paragraph shall not be in excess of 100 per centum of the excess profits net income or of the average base period net income as the case may be of the component corporation.

(7) In any case in which there is a determination of the fair market value of the properties or a determination of an allocation of excess profits net income or average base period net income based on identifiable earnings, such fair market values or excess profits net incomes or average base period net incomes so determined shall be binding upon all parties to the transactions for the excess profits tax taxable year for which determined and for all subsequent excess profits tax taxable years.

(8) Cross reference: For rules for the allocation of payroll, gross receipts, equity capital, borrowed capital, and capital additions and reductions, see sections 461 (c) (3), 462 (c), 463, and 464.

(j) (1) If, after December 31, 1945—

(A) The taxpayer acquired stock in another corporation, and thereafter such other corporation became a component corporation of the taxpayer, or

(B) A corporation (hereinafter called "first corporation") acquired stock in another corporation (hereinafter called "second corporation"), and thereafter the first and second corporations became component corporations of the taxpayer,

then to the extent that the consideration for such acquisition was not the issuance of the taxpayer's or first corporation's, as the case may be, own stock, the average base period net income of the taxpayer shall be reduced, and the transferred capital addition and reduction adjusted, in respect of the income and capital addition and reduction of the corporation whose stock was so acquired and in respect of the income and capital addition and reduction of any other corporation which at the time of such acquisition was connected directly or indirectly through stock ownership with the corporation whose stock was so acquired and which thereafter became a component corporation of the taxpayer, in such amounts and in such manner as shall be determined in accordance with regulations prescribed by the Secretary. For the purposes of this paragraph, stock which has, in the hands of the taxpayer or first corporation, as the case may be, a basis determined with reference to the basis of stock previously acquired by the issuance of the taxpayer's or first corporation's, as the case may be, own stock, shall be considered as having been acquired in consideration of the issuance of the taxpayer's or first corporation's, as the case may be, own stock.

(2) If during the taxable year for which tax is computed under this subchapter the taxpayer acquires assets in a transaction which constitutes it an acquiring corporation, the amount includible under subsection (a), attributable to such transaction, shall be limited to an amount which bears the same ratio to the amount computed without regard to this subsection as the number of days in the taxable year after such transaction bears to the total number of days in such taxable year.

(k) In the case of a partnership which is a component corporation by virtue of section 461 (b) (5) and (6), the computations required by this part shall be made, under rules and regulations prescribed by the Secretary, as if such partnership had been a corporation.

(l) In the case of a taxpayer which becomes an acquiring corporation in any taxable year ending after June 30, 1950, if, at the beginning of the first taxable year of such corporation which ends after June 30, 1950, and at all times until the taxpayer became an acquiring corporation—

(1) The taxpayer owned not less than 75 per centum of each class of stock of each of the qualified component corporations involved in the transaction in which the taxpayer became an acquiring corporation; or

(2) One of the qualified component corporations involved in the transaction owned not less than 75 per centum of each class of stock of the taxpayer, and of each of the other qualified component corporations involved in the transaction,

the average base period net income of the taxpayer shall not be less than (A) the average base period net income of that one of its qualified component corporations involved in the transaction the average base period net income of which is greatest, or (B) the average base period net income of the taxpayer computed without regard to the base period net income of any of its qualified component corporations involved in the transaction. As used in this subsection, the term "qualified component corporation" means a component corporation which was in existence and had commenced business (without regard to the provisions of section 461 (d)) on the date of the beginning of the taxpayer's base period.

(m) *Treatment of abnormalities in income in taxable period.* In the case where an acquiring corporation in a transaction described in section 461 (a) which occurred on or before December 31, 1950, receives income which, under the provisions of section 456 (relating to abnormalities in income in taxable period), would be attributable, under section 456 (b), to a taxable year of a component corporation of such acquiring corporation, which taxable year closed prior to or with the close of the base period of the acquiring corporation, for purposes of section 456, such income, and all other income of the same class, of the component corporation for such year and previous taxable years shall be treated as income of the acquiring corporation.

SEC. 463. CAPITAL CHANGES.

(a) *Taxpayer using part II of this subchapter.* For the purposes of section 435 (g), if the transaction which constitutes a taxpayer an acquiring corporation occurs in a taxable year of the taxpayer which ends after June 30, 1950, and the taxpayer's average base period net income is computed by application of this part, the following rules shall apply in computing the net capital addition and net capital reduction of such acquiring corporation after such transaction:

(1) Except with respect to a transaction described in section 461 (a) (1) (E), in the determination of the amounts of money and property paid in for stock or as paid in surplus or as a contribution to capital after the beginning of the taxable year of the acquiring corporation for the purposes of section 435 (g) (3) (A), there shall be added, as of the day after the transaction, the amounts of money and property paid in for stock or as paid in surplus or as a contribution to capital to a component corporation after the beginning of the taxable year of such component corporation and prior to the day of the transaction which constitutes such corporation a component corporation.

(2) Except with respect to a transaction described in section 461 (a) (1) (E), in the determination of the amounts of distributions to shareholders which were not out of the earnings and profits of the taxable year of the acquiring corporation for the purposes of section 435 (g) (4) (A), there shall be added, as of the day after the transaction, the amounts of distributions to shareholders of a component corporation not out of the earnings and profits of its taxable year in which such transaction occurred and prior to such day.

(3) Except with respect to a transaction described in section 461 (a) (1) (E), for the purpose of section 435 (g) (3) (B) and (g) (4) (B), for a taxable year of the acquiring corporation beginning after the date of the transaction the equity capital of the acquiring corporation at the beginning of the taxpayer's first taxable year under this subchapter shall be the aggregate of the equity capital of the acquiring corporation as of such date and the equity capital of a component corporation as of the first day of the first taxable year of such component corporation under this subchapter. This rule shall be modified pursuant to regulations prescribed by the Secretary under section 462 (j) to the extent that the transaction is subject to that subsection.

(4) Except with respect to a transaction described in section 461 (a) (1) (E), in the case of the taxable year in which the transaction occurred, for purposes of section 435 (g) (3), there shall be added as of the day of the transaction the amount, if any, by which the equity capital of a component corporation at the beginning of its taxable year in which the transaction occurred exceeds its equity capital at the beginning of its first taxable year under this subchapter, and, for purposes of section 435 (g) (4), there shall be added as of the day of the transaction the amount, if any, by which the equity capital of a component corporation at the beginning of its first taxable year under this subchapter exceeds its equity capital at the beginning of its taxable year in which the transaction occurred.

(5) Except in the case of a transaction described in section 461 (a) (1) (E), for the purposes of section 435 (g) (3) (C) and (g) (4) (C), in the computation of the daily borrowed capital of the acquiring corporation for the first day of such corporation's first taxable year under this subchapter there shall be added the daily borrowed capital of a component corporation for the first day of its first taxable year under this subchapter, and in the computation of the average borrowed capital of the acquiring corporation for its taxable year in which such transaction occurred there shall be included the daily borrowed capital of a component corporation for that part of the acquiring corporation's taxable year prior to the transaction.

(6) Except in the case of a transaction described in section 461 (a) (1) (E), for the purposes of section 435 (g) (5) (C) and (D), in the computation of the original inadmissible assets of the acquiring corporation there shall be added the original inadmissible assets of a component corporation, and in the computation of the average inadmissible assets of the acquiring corporation for the taxable year of the transaction there shall be added the daily amounts attributable to the inadmissible assets of a component corporation for that part of the acquiring corporation's taxable year prior to the date of the transaction.

(7) The Secretary shall prescribe by regulation such modification of the rules specified in this section as may be necessary to carry out the principles of such rules and the rules of section 435 (g) in cases involving intercorporate stock ownership, contributions, distributions, stock purchases, and loans between parties to a transaction described in section 461 (a), or their shareholders, prior to the date of such transaction.

(8) In the case of an acquiring corporation in a transaction described in section 461 (a) (1) (E), for the purposes of section 435 (g) (3) (B) and (g) (4) (B), so much of the equity capital of the component corporation at the beginning of its first taxable year under this subchapter shall be allocated to the acquiring corporation as is proportionate to the ratio which the equity capital transferred to the acquiring corporation in the transaction bears to the equity capital of the component corporation immediately prior to the transaction. The amount so allocated shall be deemed to be the equity capital of the taxpayer as of the first day of its first taxable year under this subchapter. For purposes of sections 435 (g) (3) (B) and 435 (g) (4) (B) the equity capital of the acquiring corporation at the beginning of its taxable year in which the transaction occurred shall be computed as of the day following the transaction.

(9) In the case of a transaction described in section 461 (a) (1) (E), for the purposes of section 435 (g) (3) (C) and (g) (4) (C), the daily borrowed capital of an acquiring corporation for the first day of such corporation's first taxable year under this subchapter shall be such portion of the daily borrowed capital of the component corporation for the first day of its first taxable year under this subchapter as the borrowed capital of the acquiring corporation immediately after the transaction bears to the borrowed capital of the component corporation as of the close of the day prior to the day of the transaction.

(10) In the case of a transaction described in section 461 (a) (1) (E), in the determination of the original inadmissible assets of an acquiring corporation for the purposes of section 435 (g) (5) (C) and (g) (5) (D), there shall be allocated to such corporation that proportion of the original inadmissible assets of the component corporation as is proportionate to the ratio which the inadmissible assets transferred to the acquiring corporation in the transaction bears to the total of the inadmissible assets held by the component corporation immediately prior to the transaction. The amount so allocated shall be deemed to be the original inadmissible assets of the acquiring corporation.

(11) For purposes of the determination under section 435 (g) (6) and (7) of the amount to be added to the daily capital reduction in the case of a corporation a member of a controlled group such determination shall be made, pursuant to regulations prescribed by the Secretary, in a manner consistent with the method provided in such sections.

(12) In the case of a transaction other than that described in section 461 (a) (1) (E), to the extent that stock of a component corporation was acquired in an exchange for other than stock of the acquiring corporation within the meaning of section 462 (j), the basis of the assets of the component corporation shall be redetermined as provided in section 470 and such redetermination basis shall be used for all purposes of section 435 (g).

(13) In the case of transactions described in section 462 (e) (1) (C), (e) (1) (B), and (e) (2) the net capital additions and reductions of the acquiring corporation after the transaction shall be determined under this section subject to the application, prior to the transaction, of section 443 (d) to each corporation which was a party to the transaction.

(14) In the case of transactions described in section 462 (g) (2) and the second sentence of (g) (3), the net capital additions and reductions of the acquiring corporation after the transaction shall be determined under this section subject to the application, prior to the transaction, of section 445 (f) to each corporation which was a party to the transaction.

(b) *Rule where acquiring corporation is component of taxpayer.* In cases where an acquiring corporation is a component of the taxpayer, and the transaction which constitutes such corporation an acquiring corporation occurs in a taxable year of such corporation which ends after June 30, 1950, for the purpose of determining the daily capital addition or reduction of the taxpayer the above rules shall be applied in a similar manner to determine the net capital addition or reduction of such acquiring corporation for each day after such transaction.

SEC. 464. CAPITAL CHANGES DURING THE BASE PERIOD.

For the purposes of section 435 (f), if the transaction which constitutes the taxpayer an acquiring corporation occurred during or after the beginning of the second taxable year preceding the first taxable year of the acquiring corporation under this subchapter, and the acquiring corporation's average base period net income is computed by application of this part, the following rules shall apply in computing the base period capital addition of such acquiring corporation:

(a) In the case of a transaction, other than a transaction described in section 461 (a) (1) (E), which—

(1) Occurred during or after the first taxable year of the acquiring corporation under this subchapter, for the purposes of section 435 (f), the base period capital addition of the acquiring corporation for the taxable year in which the transaction occurred shall be the sum of:

(A) The base period capital addition of the acquiring corporation, and

(B) So much of the base period capital addition of a component corporation as is proportionate to the ratio which the number of days in the taxable year of the acquiring corporation after the transaction bears to the number of days in such taxable year;

and the base period capital addition of the acquiring corporation for any taxable year thereafter shall be the aggregate of the base period capital addition of the acquiring corporation and the base period capital addition of such component corporation.

(2) Occurred during the taxable year of the acquiring corporation immediately preceding its first taxable year under this subchapter, its base period capital addition shall be computed after—

(A) Adding to its yearly base period capital for the immediately preceding taxable year (as defined in section 435 (f) (2) (A) (ii)) of the acquiring corporation the yearly base period capital for the immediately preceding taxable year (so defined) of a component corporation, and

(B) Adding to its yearly base period capital for the second preceding taxable year (as defined in section 435 (f) (2) (A) (iii)) of the acquiring corporation the yearly base period capital for the second preceding taxable year (so defined) of such component corporation.

(3) Occurred during the second taxable year of the acquiring corporation preceding its first taxable year under this subchapter, its base period capital addition shall be computed after adding to its yearly base period capital for the second preceding taxable year (as defined in section 435 (f) (2) (A) (iii)) of the acquiring corporation the yearly base period capital for the second preceding taxable year (so defined) of a component corporation.

(b) In the case of a transaction described in section 461 (a) (1) (E) which—

(1) Occurred during or after the first taxable year of the component corporation under this subchapter, for purposes of section 435 (f), the base period capital addition of the acquiring corporation shall be such portion of the base period capital addition of the component corporation as is proportionate to the ratio which the fair market value of the assets transferred to the acquiring corporation in the transaction bears to the fair market value of the assets of a component corporation immediately prior to the transaction;

(2) Occurred during a taxable year of the component corporation which is or would be if it remained in existence, a taxable year preceding its first taxable year under this subchapter.

(A) The yearly base period capital of the acquiring corporation for the year in which the transaction occurred shall be computed as of the day following the transaction.

(B) If the taxable year of the acquiring corporation during which the transaction occurred is its first taxable year under this subchapter, its base period capital addition shall be computed by

(i) Treating as its yearly base period capital for the immediately preceding taxable year (as defined in section 435 (f) (2) (ii)) such portion of the yearly base period capital of the component corporation for the first day of the taxable year of the component corporation in which such transaction occurred, and

(ii) Treating as its yearly base period capital for the second preceding taxable year (as defined in section 435 (f) (2) (iii)) such portion of the yearly base period capital of the component corporation for the first day of the taxable year of the component corporation before the taxable year of the component corporation in which the transaction occurred as is proportionate to the ratio which the fair market value of the assets transferred to the acquiring corporation in the transaction bears to the fair market value of the assets of the component corporation immediately prior to the transaction.

(C) If the taxable year of the acquiring corporation during which the transaction occurred is its taxable year immediately preceding its first taxable year under this subchapter its base period capital addition shall be computed by treating as its yearly base period capital for the second preceding taxable years (as defined in section 435 (f) (2) (iii)) such portion of the base period capital of the component corporation for the first day of the taxable year of the component corporation in which such transaction occurred as is proportionate to the ratio which the fair market value of the assets transferred to the acquiring corporation in the transaction bears to the fair market value of the assets of the component corporation immediately prior to the transaction.

(3) Was a transaction in which a part of the assets of a component corporation were transferred to an acquiring corporation which had commenced business prior to such transaction, the base period capital addition of such acquiring corporation shall be computed pursuant to regulations prescribed by the Secretary.

SEC. 465. FOREIGN CORPORATIONS.

The term "corporation" as used in this part does not include a foreign corporation.

PART III—INVESTED CAPITAL IN CONNECTION WITH CERTAIN EXCHANGES AND LIQUIDATIONS

SEC. 470. ADJUSTED BASIS OF ASSETS RECEIVED IN CERTAIN INTERCORPORATE LIQUIDATIONS.

For the purposes of this subchapter (other than section 458)—

(a) *Basis of assets acquired in intercorporate liquidation.* The property received by a transferee in an intercorporate liquidation attributable to a share of stock having in the hands of the transferee a basis determined to be a cost basis, shall be considered to have an adjusted basis at the time so received determined as follows:

(1) The aggregate of the property (other than money) held by the transferor at the time of the acquisition by the transferee of control of the transferor (or, if such share was acquired after the acquisition of such control, at the time of the acquisition of such share, or, if such control was not acquired, at the time immediately prior to the receipt of any property in the intercorporate liquidation in respect of such share) shall be deemed to have an aggregate basis equal to the amount obtained by (A) multiplying the amount of the adjusted basis at such time of such share in the hands of the transferee by the aggregate number of share units in the transferor at such time (the interest represented by such share being taken as the share unit), and (B) adjusting for the amount of money on hand and the liabilities of the transferor at such time.

(2) The basis which property of the transferor is deemed to have under paragraph (1) at the time therein specified shall be used in determining the basis of property subsequently acquired by the transferor the basis of which is determined with reference to the basis of property specified in paragraph (1).

(3) The basis which property of the transferor is deemed to have under paragraphs (1) and (2) at the time therein specified shall be used in determining all subsequent adjustments to the basis of such property.

(4) The property so received by the transferee shall be deemed to have, at the time of its receipt, the same basis it is deemed to have under the foregoing provisions of this subsection in the hands of the transferor, or in the case of property not specified in paragraph (1) or (2), the same basis it would have had in the hands of the transferor.

(5) Only such part of the aggregate property received by the transferee in the intercorporate liquidation as is attributable to such share shall be considered as having the adjusted basis which property is deemed to have under paragraphs (1), (2), (3), and (4) of this subsection.

(b) *Basis for equity capital credit.* The adjusted basis which property received by the transferee in an intercorporate liquidation is considered to have under the provisions of subsection (a) at the time of its receipt shall be thereafter treated as the adjusted basis, in lieu of the adjusted basis otherwise prescribed, in computing any amount, determined by reference to the basis of such property in the hands of the transferee, entering into the computation of the equity capital of the transferee, or of any other corporation the computation of the equity capital of which is determined by reference to the basis of such property in the hands of the transferee.

(c) *Statutory mergers and consolidations.* If a corporation owns stock in another corporation and such corporations are merged or consolidated in a statutory merger or consolidation, then for the purposes of this section and section 437 such stock shall be considered to have been acquired (in such statutory merger or consolidation) by the corporation resulting from the statutory merger or consolidation, and the properties of such other corporation attributable to such stock to have been received by such resulting corporation as a transferee from such other corporation as a transferor in an intercorporate liquidation.

(d) *Determinations*—(1) *Regulations.* Any determination which is required to be made under this section (including determinations in applying this section in cases where there is a series of transferees of the property and cases where the stock of the transferor is acquired by the transferee from another corporation, and the determination of the basis and adjusted basis which property or items thereof have or are considered to have) shall be made in accordance with regulations which shall be prescribed by the Secretary. If the transferor or the transferee is a foreign corporation, the provisions of this section shall apply to such extent and under such conditions and limitations as may be provided in such regulations.

(2) *Application to liquidation extending over long period.* The Secretary is authorized to prescribe rules similar to those provided in this section with respect to the days within the period beginning with the date on which the first property is received in the intercorporate liquidation and ending with the day of its completion; and the extent to which, and the conditions and limitations under which such rules are to be applicable.

(e) *Definitions*—(1) *Intercorporate liquidation.* As used in this section, the term "intercorporate liquidation" means the receipt (whether or not after December 31, 1949) by a corporation (hereinafter called

the "transferee") of property in complete liquidation of another corporation (hereinafter called the "transferor") to which

(A) The provisions of section 112 (b) (6), or the corresponding provision of a prior revenue law, is applicable or

(B) A provision of law is applicable prescribing the nonrecognition of gain or loss in whole or in part upon such receipt (including a provision of the regulations applicable to a consolidated income or excess profits tax return but not including section 112 (b) (7), (9), or (10) or a corresponding provision of a prior revenue law),

but only if none of such property so received is a stock or a security in a corporation the stock or securities of which are specified in the law applicable to the receipt of such property as stock or securities permitted to be received (or which would be permitted to be received if they were the sole consideration) without the recognition of gain.

(2) *Control.* As used in this section, the term "control" means the ownership of stock possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the ownership of at least 80 per centum of the total number of shares of all other classes of stock (except nonvoting stock which is limited and preferred as to dividends), but only if in both cases such ownership continues until the completion of the intercorporate liquidation.

§ 40.470–1 *Adjusted basis of assets received in certain intercorporate liquidations.* Section 470 provides specific rules applicable in determining the adjusted basis of assets received in certain intercorporate liquidations. These rules must be applied for all purposes of the excess profits tax except the computations under section 458, relating to the historical invested capital. These rules shall be applied in a manner consistent, to the extent appropriate, with the principles of the regulations relating to the corresponding rules provided in section 472.

SEC. 471. EXCHANGES.

For purposes of section 458—

(a) *Definitions, Etc.* For the purposes of this section—

(1) *"Exchange", "transferor", and "transferee".* The term "exchange" means a transaction by which one corporation (hereinafter called "transferee") receives property of another corporation (hereinafter called "transferor") and the basis of the property received, in the hands of the transferee, for the purposes of section 458 (d) is determined by reference to the basis in the hands of the transferor.

(2) *Determination of basis of property received.* The basis, in the hands of the transferee, of the property of the transferor received by the transferee upon the exchange shall be determined in accordance with section 458 (d).

(b) *Rule.* In the application of section 458 (d) to a transferee upon an exchange in determining the amount paid in for stock of the transferee, or as paid-in surplus or as a contribution to capital of the transferee, in connection with such exchange, only an amount shall be deemed to have been so paid in equal to the excess of the basis in the hands of the transferee of the property of the transferor received by the transferee upon the exchange over the sum of—

(1) The amount of any liability of the transferor assumed upon the exchange and of any liability subject to which such property was so received, plus

(2) The amount of any liability of the transferee (not arising out of any liability described in paragraph (1)) constituting consideration for the property so received, plus

(3) The aggregate of the amount of any money and the fair market value of any other property (other than such stock and other than property described in paragraphs (1) and (2)) transferred to the transferor.

(c) *Reduction in daily invested capital.* In the application of section 458 (c) to a transferee upon an exchange, the daily invested capital for any day after such exchange shall be reduced by an amount equal to the amount by which the sum of the amounts specified in paragraphs (1), (2), and (3) of subsection (b) exceeds the basis in the hands of the transferee of the property of the transferor received upon the exchange.

§ 40.471–1 *Definitions and determinations.* For the purposes of section 471 and of §§ 40.471–1, 40.471–2, and 40.471–3:

(a) *Exchange, transferee, transferor.* The term "exchange" means a transaction in which one corporation, called the "transferee," acquires property of another corporation, called the "transferor," and the basis to the transferee of the property acquired, for the purposes of determining the amount of money or property paid in for stock, or as paid-in surplus, or as a contribution to the captial of the transferee pursuant to the provisions of section 458 (d) as a result of such exchange, is a substituted basis under section 113 (b) (2) (A), i. e., is a basis determined by reference to the basis of such property in the hands of the transferor.

(b) *Applicability of section 471 to various types of exchanges*—(1) *In general.* A substituted basis within the provisions of section 113 (b) (2) (A) may result from—

(i) The application of section 113 (a) (7) to property acquired in an exchange in a taxable year beginning after December 31, 1917, pursuant to a plan of reorganization under the provisions of section 112 (g);

(ii) The application of section 113 (a) (8) to property acquired in a taxable year beginning after December 31, 1920, by a corporation by the issuance of its stock or securities, if immediately after such acquisition the transferor is in control of the corporation under the provisions of section 112 (b) (5), or by a corporation as paid-in surplus or as a contribution to capital;

(iii) The application of section 113 (a) (17) and section 372 in certain instances to property acquired in connection with exchanges and distributions in obedience to certain orders of the Securities and Exchange Commission;

(iv) The application of section 113 (a) (20) to property acquired in certain railroad reorganizations;

(v) The application of section 113 (a) (21) to property acquired by certain street, suburban, or interurban electric railway corporations;

(vi) The application of section 113 (a) (22) to property acquired in a taxable year beginning after December 31, 1933, in a reorganization of a corporation resulting from certain receivership and bankruptcy proceedings; and

(vii) The application of a provision of consolidated returns regulations to property acquired by a member of an affiliated group of corporations from another member of such group during a consolidated return period.

The rules provided with respect to the provisions of the Code mentioned in this section shall also be applicable with respect to corresponding provisions of prior revenue laws.

*Example.* In 1939 Corporation X, solely in exchange for 1,000 shares of its common voting stock (representing 5 percent of its total voting stock), acquired in a statutory reorganization under section 112 (g) (1) (C) all the assets of Corporation Y. Under section 113 (a) (7), (B), the basis of such assets in the hands of Corporation X would be determined by reference to the basis of such assets in the hands of Corporation Y. The amount to be included in the equity invested capital of Corporation X as the amount paid in for stock of Corporation X as a result of such exchange shall be determined under section 471.

The mere fact that property was acquired in an exchange pursuant to a plan of reorganization in which gain or loss was not recognized does not of itself invoke the provisions of section 471 if the basis of the property is not fixed by reference to the basis in the hands of the transferor. Thus, if the exchange described in the preceding example occurred in 1935, the basis of the assets to Corporation X would be fair market value at the date of the exchange because of failure of Corporation Y to retain the 50 percent control in such assets pursuant to section 113 (a) (7) (A), and the provisions of section 471 would be inapplicable in determining the amount includible in the equity invested capital of Corporation X as a result of the exchange.

(2) *Exchanges constituting intercorporate liquidations.* Since section 471 is applicable only in the determination of the amount paid in for stock, or as paid-in surplus, or as a contribution to capital, of a transferee upon an exchange, such section shall not be applicable in determining the equity invested capital of such transferee in the case of the receipt of property in any of the exchanges described in this section if the receipt of such property is a distribution in an intercorporate liquidation, in whole or in part, of the transferor within the provisions of section 472. In such cases, the exchange shall be considered to be an intercorporate liquidation subject to the provisions of section 472. For rules relating to the adjustment of equity invested capital in the case of intercorporate liquidations, see section 472 and § 40.472–7.

*Example.* Prior to 1940, Corporation A owned the entire outstanding capital stock of Corporation B. In 1940, Corporation C acquired all of the assets of Corporation A and Corporation B in a statutory consolidation constituting a reorganization under section 112 (g) (1) (A). Although Corporation C might be deemed to have acquired the assets of Corporation B with a basis determined by reference to the basis of such assets in the hands of Corporation B, the provisions of section 471 are not applicable to such exchange since section 472 (f) provides that, in such a case, Corporation C shall be considered to have acquired in the statutory consolidation the stock of Corporation B previously owned by Corporation A and to have received the assets of Corporation B in an intercorporate liquidation.

(c) *Determination of basis of property received*—(1) *General rule.* In determining the amount paid in for stock, or as paid-in surplus, or as a contribution to capital of the transferee for the purposes of section 458 (d) with respect

to an exchange, the basis of the property received upon the exchange is to be determined in accordance with the rules provided by section 458 (d) (2), namely, the basis (unadjusted) to the transferee for determining loss, adjusted with respect to the period prior to its receipt by the transferee, by an amount equal to the adjustments proper under section 115 (l) for determining earnings and profits. For the purposes of determining such basis (unadjusted) to the transferee, the amount of any gain or loss recognized to the transferor upon the exchange shall be limited to the gain or loss taken into account under section 115 (l) in computing the earnings and profits of the transferor. If the property was not disposed of prior to the taxable year, such unadjusted basis shall be determined under the law applicable to the taxable year. If the property was acquired in a taxable year beginning after February 28, 1913, and prior to January 1, 1934, and the basis of such property was prescribed by section 113 (a) (6), (7), or (9) of the Revenue Act of 1932, or if the property was acquired in a taxable year beginning after February 28, 1913, and prior to January 1, 1936, and the basis of such property was prescribed by section 113 (a) (6), (7), or (8) of the Revenue Act of 1934, for the purposes of section 471 the basis of such property shall be the same as the basis prescribed by the Revenue Act of 1932 or the Revenue Act of 1934, respectively. See section 113 (a) (12) and (16). If the property was disposed of prior to the taxable year, such unadjusted basis shall be that prescribed by the law applicable to the year of disposition, but without regard to the value of the property as of March 1, 1913.

(2) *Applicability of section 471 in case of statutory change.* If the transferee received property in any taxable year in a transaction which, under the revenue law applicable to such year, did not constitute an exchange within the provisions of section 471 (a), and if—

(i) Such property is held in the taxable year, and under the revenue law applicable to such year such transaction qualifies as an exchange under section 471, or

(ii) Such property was disposed of in a taxable year subsequent to the year of acquisition and under the revenue law applicable to such subsequent taxable year, the transaction did qualify as an exchange under section 471,

the provisions of section 471 are applicable in determining the amount paid in to the transferee as a result of such transaction. However, if such property was disposed of prior to a year in which the revenue law was changed so as to bring a transaction of such a character within the provisions of section 471, the provisions of section 471 shall not be applicable in determining the invested capital of the transferee attributable to the property acquired in such transaction.

Thus, if after December 31, 1917, a corporation acquired the entire assets of another corporation in exchange solely for 79 percent of its voting stock, although such transaction would constitute a reorganization and a tax-free exchange under the Revenue Acts of 1924, 1926, and 1928, the basis of the assets to the transferee would not be determined by reference to the basis of such assets in the hands of the transferor since an interest or control of 80 percent in the assets transferred did not remain in the transferor. See sections 203 (b) (3) and (4), 203 (h) (1) (A), and 204 (a) (7) of the Revenue Acts of 1924 and 1926, and sections 112 (b) (3) and (4), 112 (i) (1) (A), and 113 (a) (7) of the Revenue Act of 1928. The percentage of control necessary to establish a substituted basis for such property was reduced to 50 percent by section 113 (a) (7) of the Revenue Acts of 1932 and 1934. The Revenue Act of 1936 removed the necessity for any control under section 113 (a) (7), but preserved the basis established under the Revenue Act of 1932 or 1934. The Revenue Act of 1938 and the Code provide in section 113 (a) (7) (A) that with respect to property acquired by a corporation in connection with a reorganization after December 31, 1917, but in a taxable year beginning prior to January 1, 1936, 50 percent control is necessary for the property transferred to have a basis to the transferee fixed by reference to the basis of the property in the hands of the transferor. In the case of property acquired in connection with a reorganization after December 31, 1935, no such control is necessary.

*Example.* Assume that in 1926, Corporation C acquired all the property of Corporation D in exchange for 79 percent of its entire capital stock, all of which was voting stock. Although the transaction would have been a reorganization and a tax-free exchange, the basis of the property to Corporation C in any taxable year beginning before January 1, 1932, would not have been fixed by reference to the basis of such property in the hands of Corporation D. Consequently, if Corporation C had disposed of the property prior to January 1, 1932, the amount paid in to Corporation C as a result of the 1926 exchange would not be determined under section 471. If Corporation C had disposed of the property in a taxable year beginning subsequent to December 31, 1931, the basis of such property to Corporation C would be the basis to Corporation D, and the amount paid in to Corporation C as a result of the 1926 exchange would be computed under section 471.

(3) *Inconsistent position.* As to the effect of an inconsistent position in the determination of invested capital under section 471, or without regard to its provisions, see section 452 and the regulations thereunder.

§ 40.471–2 *Determination of amount paid in for stock, or as paid-in surplus, or as a contribution to capital.* For the purposes of section 458 (d), the amount of money or property determined to have been paid in for stock of the transferee, or as paid-in surplus or as a contribution to capital of the transferee in connection with an exchange defined in § 40.471–1 (a) shall be the excess of the basis (determined under § 40.471–1 (b)) in the hands of the transferee of the property of the transferor received by the transferee upon the exchange over the sum of—

(a) The amount of any liability of the transferor assumed upon the exchange and of any liability subject to which such property was so received, plus

(b) The amount of any liability of the transferee (not arising out of any liability described in paragraph (a) of this section) constituting consideration for the property so received, plus

(c) The aggregate of the amount of any money and the fair market value of any other property (other than such stock and other than property described in paragraphs (a) and (b) of this section) transferred to the transferor, whether or not such money or property was permitted to be received by the transferor without the recognition of gain.

If the sum of the amounts specified in paragraphs (a), (b), and (c) of this section exceeds the basis in the hands of the transferee of the property received from the transferor, such excess shall not be taken into account in computing the equity invested capital of the transferee but shall be used to reduce the daily invested capital of the transferee for each day after the exchange. As to the computation to be made in case of such excess, see § 40.471–3.

*Example (1).* In 1950 Corporation X transferred property which had an adjusted basis for determining gain or loss of $600,000 to Corporation Y in consideration (1) of 80 percent of the capital stock of Corporation Y which had a fair market value of $400,000; (2) of the assumption by Corporation Y of open account indebtednesss of Corporation X amounting to $20,000; (3) of the payment by Corporation Y of money and other property amounting to $120,000; and (4) of the issuance by Corporation Y to Corporation X of a bond in the amount of $110,000 secured by a lien upon the property acquired. Included in the property acquired by Corporation Y in connection with the foregoing exchange was a building which was subject to a mortgage liability of $100,000 which was not assumed by Corporation X and which was not assumed by Corporation Y. The money and other property received by Corporation X was not distributed in pursuance of the plan of reorganization and therefore the gain resulting from the exchange was recognized by such corporation in accordance with section 112 (d) (2). The amount includible in the equity invested capital of Corporation Y determined under the provisions of section 471 (b) with respect to the exchange is $370,000, computed as follows:

*Gain to Corporation X Recognized Upon Exchange*

| | |
|---|---|
| Fair market value of capital stock of Corporation Y | $400,000 |
| Amount of liabilities of Corporation X assumed | 20,000 |
| Bond secured by lien upon property | 110,000 |
| Money and other property | 120,000 |
| Mortgage liability subject to which building was transferred | 100,000 |
| Total consideration | 750,000 |
| Less: Adjusted basis of property transferred | 600,000 |
| Gain | 150,000 |

The gain recognized to Corporation X, however, is limited to $120,000, representing the sum of the money and fair market value of other property received by Corporation X which, pursuant to the plan of reorganization, was not distributed (see sections 112 (d) (2) and 112 (k)).

*Amount Deemed To Be Paid in for Stock of Corporation Y Under Section 458 (d) and Section 471*

| | | |
|---|---|---|
| Adjusted basis of property to Corporation X | | $600,000 |
| Add: Gain to Corporation X recognized upon exchange | | 120,000 |
| Unadjusted basis for determining loss to Corporation Y | | 720,000 |
| Deduct: Amount of liabilities of Corporation X assumed | $20,000 | |
| Bonds issued by Corporation Y secured by lien upon property received | 110,000 | |
| Money and other property paid | 120,000 | |
| Mortgage liability subject to which building was acquired by Corporation Y | 100,000 | |
| | | 350,000 |
| Amount deemed to have been paid in for stock of Corporation Y upon the exchange | | 370,000 |

*Daily Invested Capital of Corporation Y Resulting From the Exchange*

| | | |
|---|---|---|
| Amount deemed to have been paid in to Corporation Y upon the exchange | | $370,000 |
| Borrowed invested capital: | | |
| Mortgage liability on building not assumed | $100,000 | |
| Bond issued secured by lien upon property | 110,000 | |
| Total borrowed capital | 210,000 | |
| Borrowed invested capital (75 percent of $210,000) | | 157,500 |
| Daily invested capital | | 527,500 |

Assume that in 1951, Corporation Y sold the properties acquired from Corporation X for $750,000, the purchaser paying cash in the amount of $650,000 and taking the building subject to the mortgage liability of $100,000. The gain recognized to Corporation Y, and included in its earnings and profits, is $30,000 ($750,000 minus $720,000). There were no other accumulated earnings and profits. Immediately thereafter Corporation Y redeemed and canceled the bond and mortgage it had issued to Corporation X at the time of the exchange. That portion of the daily invested capital of Corporation Y for the excess profits tax taxable year following the year of the sale and attributable to the acquisition and sale of the properties received from Corporation X would be $400,000, computed as follows:

| | |
|---|---|
| Equity invested capital resulting from the exchange | $370,000 |
| Earnings and profits from sale of properties | 30,000 |
| Daily invested capital | 400,000 |

*Example (2).* Assume that in the preceding example, the money and other property received by Corporation X upon the exchange were distributed pursuant to the plan of reorganization so that no gain was recognized to Corporation X as a result of the exchange (see sections 112 (d) (1) and 112 (k)). Consequently, the basis of the property received by Corporation Y would not be increased by any gain recognized to Corporation X pursuant to section 113 (a) (7), and would be $600,000, rather than $720,000. The amount deemed to have been paid in for stock of Corporation Y upon the exchange would be $250,000 instead of $370,000, and the daily invested capital of Corporation Y resulting from the exchange would be $407,500 instead of $527,500. Upon the sale of the property, however, a gain of $150,000, rather than $30,000, would be realized, and the accumulated earnings and profits of Corporation Y would be increased accordingly by $150,000 instead of $30,000. That portion of the daily invested capital of Corporation Y for the excess profits tax taxable year following the year of the sale and attributable to the acquisition and sale of the properties received from Corporation X would be $400,000 ($250,000 plus $150,000).

§ 40.471–3 *Reduction in daily invested capital.* For the purposes of determining the daily invested capital of the transferee upon an exchange pursuant to the provisions of section 458 (c) for any day after such exchange, the daily invested capital for each such day shall be reduced by an amount equal to the excess of the sum of the amounts specified in section 471 (b) (1), (2), and (3) over the basis (determined in accordance with § 40.471–1 (b)) to the transferee of the property of the transferor received upon the exchange.

In any case in which the excess of the sum of the amounts specified in section 471 (b) (1), (2), and (3) over the basis of the transferee of the property received upon the exchange is greater than the amount of the daily invested capital for any day after such exchange, the daily invested capital for such day shall be a minus quantity. In such case the average invested capital of the taxpayer computed under section 458 (b) shall be the aggregate of the daily invested capital for each day of the taxable year computed by taking into account any plus amounts in daily invested capital and any negative amounts in daily invested capital after the exchange resulting from the application of section 471 (c), divided by the number of days in such taxable year. In no case, however, shall such average invested capital be an amount which is less than zero.

*Example (1).* In 1951 Corporation O owned property with an adjusted basis for determining gain or loss of $400,000 but with a fair market value of $1,000,000. Corporation O had no accumulated earnings and profits or deficit in earnings and profits. On June 30, 1951, pursuant to a plan of reorganization, Corporation P acquired such property from Corporation O in exchange for 80 percent of its outstanding stock which had a fair market value of $400,000, $125,000 in cash, and $475,000 of its short-term notes. Immediately prior to the exchange Corporation P had an equity invested capital of $100,000, consisting of money and property paid in and of accumulated earnings and profits. Under section 112 (d) (1) no gain was recognized to Corporation O upon the exchange since immediately after the exchange and in pursuance of the plan of reorganization it distributed the cash and stock and notes of Corporation P to its shareholders. The daily invested capital of Corporation P for each day after the exchange was $256,250 and the average invested capital for the taxable year 1951 was $178,767, computed as follows:

*Daily Invested Capital of Corporation P Immediately After Exchange*

| | | |
|---|---|---|
| Equity invested capital immediately prior to exchange | | $100,000 |
| Amount deemed to have been paid in under sections 458 (d) and 471 upon the exchange | | 0 |
| Borrowed invested capital of Corporation P (75 percent of $475,000) | | 356,250 |
| Total daily invested capital prior to application of section 471 (c) | | 456,250 |
| Less: Amount provided by section 471 (c) as reduction in daily invested capital: | | |
| Cash paid upon the exchange | $125,000 | |
| Notes issued by Corporation P | 475,000 | |
| Total | 600,000 | |
| Less: Basis of property received upon exchange | 400,000 | |
| Reduction under section 471 (c) | | 200,000 |
| Daily invested capital for each day after exchange | | 256,250 |

*Average Invested Capital of Corporation P for 1951*

| | |
|---|---|
| Aggregate of daily invested capital for each day prior to and including the day of the exchange ($100,000 × 181 days) | $18,100,000 |
| Aggregate of daily invested capital for each day after the exchange ($256,250 × 184 days) | 47,150,000 |
| Total aggregate daily invested capital for each day of the taxable year | 65,250,000 |
| Average invested capital ($65,250,000 divided by 365 days) | 178,767 |

*Example (2)* In 1951 Corporation A owned property with an adjusted basis for determining gain or loss of $1,300,000 but with a fair market value of $7,500,000. Corporation A had no accumulated earnings and profits or deficit in earnings and profits. On June 30, 1951, pursuant to a plan of reorganization Corporation B acquired such property from Corporation A in exchange for 80 percent of its outstanding stock which had a fair market value of $1,500,000, cash of $500,000, and bonds of $5,500,000. Immediately prior to the exchange Corporation B had an equity invested capital of $375,000 consisting of money paid in and of accumulated earnings and profits. Under section 112 (d) (1) no gain was recognized to Corporation A upon the exchange since immediately after the exchange and pursuant to the plan of reorganization it distributed the

cash and bonds of Corporation B to its shareholders. The daily invested capital of Corporation B for each day after the exchange is minus $200,000 and the average invested capital for the taxable year 1951 is $85,137, computed as follows:

| | |
|---|---|
| *Daily Invested Capital Immediately After the Exchange* | |
| Equity invested capital of Corporation B immediately prior to the exchange | $375,000 |
| Amount deemed to have been paid in upon the exchange | 0 |
| Borrowed invested capital (75 percent of $5,500,000) | 4,125,000 |
| Total daily invested capital prior to application of section 471 (c) | 4,500,000 |
| Less: Amount provided by section 471 (c) as reduction in daily invested capital: | |
| Cash paid upon the exchange | $500,000 |
| Bonds issued upon the exchange | 5,500,000 |
| Total | 6,000,000 |
| Less basis of property received upon exchange | 1,300,000 |
| Reduction under section 471 (c) | 4,700,000 |
| Daily invested capital for each day immediately after exchange (a minus quantity) | (200,000) |
| *Average Invested Capital of Corporation B for 1951* | |
| Aggregate of daily invested capital for each day prior to and including the day of the exchange ($375,000×181 days) | $67,875,000 |
| Aggregate of daily invested capital for each day after the exchange (($200,000)×184 days) (a minus quantity) | (36,800,000) |
| Total aggregate daily invested capital for each day of the taxable year | 31,075,000 |
| Average invested capital ($31,075,000 divided by 365 days) | 85,137 |

SEC. 472. INVESTED CAPITAL ADJUSTMENT AT THE TIME OF TAX-FREE INTERCORPORATE LIQUIDATIONS.

For purposes of section 458—

(a) *Definition of intercorporate liquidation.* As used in this section, the term "intercorporate liquidation" means the receipt (whether or not after June 30, 1950) by a corporation (hereinafter called the "transferee") of property in complete liquidation of another corporation (hereinafter called the "transferor"), to which—

(1) The provisions of section 112 (b) (6), or the corresponding provision of a prior revenue law, is applicable or

(2) A provision of law is applicable prescribing the nonrecognition of gain or loss in whole or in part upon such receipt (including a provision of the regulations applicable to a consolidated income or excess profits tax return but not including section 112 (b) (7), (9), or (10) or a corresponding provision of a prior revenue law),

but only if none of such property so received is a stock or a security in a corporation the stock or securities of which are specified in the law applicable to the receipt of such property as stock or securities permitted to be received (or which would be permitted to be received if they were the sole consideration) without the recognition of gain.

(b) *Definition of plus adjustment and minus adjustment.* For the purposes of this section—

(1) *Plus adjustment.* The term "plus adjustment" means the amount, with respect to an intercorporate liquidation, determined to be equal to the amount by which the aggregate of the amount of money received by the transferee in such intercorporate liquidation, and of the adjusted basis at the time of such receipt of all property (other than money) so received, exceeds the sum of—

(A) The aggregate of the adjusted basis of each share of stock with respect to which such property was received; such adjusted basis of each share to be determined immediately prior to the receipt of any property in such liquidation with respect to such share, and

(B) The aggregate of the liabilities of the transferor assumed by the transferee in connection with the receipt of such property, of the liabilities (not assumed by the transferee) to which such property so received was subject, and of any other consideration (other than the stock with respect to which such property was received) given by the transferee for such property so received.

(2) *Minus adjustment.* The term "minus adjustment" means the amount, with respect to an intercorporate liquidation, determined to be equal to the amount by which the sum of—

(A) The aggregate of the adjusted basis of each share of stock with respect to which such property was received; such adjusted basis of each share to be determined immediately prior to the receipt of any property in such liquidation with respect to such share, and

(B) The aggregate of the liabilities of the transferor assumed by the transferee in connection with the receipt of such property, of the liabilities (not assumed by the transferee) to which such property so received was subject, and of any other consideration (other than the stock with respect to which such property was received) given by the transferee for such property so received

exceeds the aggregate of the amount of the money so received and of the adjusted basis, at the time of receipt, of all property (other than money) so received.

(3) *Rules for application of paragraphs (1) and (2).* In determining the plus adjustment or minus adjustment with respect to any share, the computation shall be made in the same manner as is prescribed in paragraphs (1) and (2) of this subsection, except that there shall be brought into account only that part of each item which is determined to be attributable to such share.

(c) *Rules for the application of this section*—(1) *Stock having cost basis.* The property received by a transferee in an intercorporate liquidation attributable to a share of stock having in the hands of the transferee a basis determined to be a cost basis, shall be considered to have, for the purposes of subsection (b), an adjusted basis at the time so received determined as follows:

(A) The aggregate of the property (other than money) held by the transferor at the time of the acquisition by the transferee of control of the transferor (or, if such share was acquired after the acquisition of such control, at the time of the acquisition of such share, or, if such control was not acquired, at the time immediately prior to the receipt of any property in the intercorporate liquidation in respect of such share) shall be deemed to have an aggregate basis equal to the amount obtained by (i) multiplying the amount of the adjusted basis at such time of such share in the hands of the transferee by the aggregate number of share units in the transferor at such time (the interest represented by such share being taken as the share unit), and (ii) adjusting for the amount of money on hand and the liabilities of the transferor at such time.

(B) The basis which property of the transferor is deemed to have under subparagraph (A) at the time therein specified shall be used in determining the basis of property subsequently acquired by the transferor the basis of which is determined with reference to the basis of property specified in subparagraph (A).

(C) The basis which property of the transferor is deemed to have under subparagraphs (A) and (B) at the time therein specified shall be used in determining all subsequent adjustments to the basis of such property.

(D) The property so received by the transferee shall be deemed to have, at the time of its receipt, the same basis it is deemed to have under the foregoing provisions of this paragraph in the hands of the transferor, or in the case of property not specified in subparagraphs (A) or (B), the same basis it would have had in the hands of the transferor.

(E) Only such part of the aggregate property received by the transferee in the intercorporate liquidation as is attributable to such share shall be considered as having the adjusted basis which property is deemed to have under subparagraphs (A), (B), (C), and (D) of this paragraph.

(2) *Basis of stock not a cost basis.* The property received by a transferee in an intercorporate liquidation attributable to a share of stock having in the hands of the transferee a basis determined to be a basis other than a cost basis shall, for the purposes of subsection (b), be considered to have, at the time of its receipt, the basis it would have had had the first sentence of section 113 (a) (15) been applicable.

(3) *Definition of control.* As used in this subsection, the term "control" means the ownership of stock possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the ownership of at least 80 per centum of the total number of shares of all other classes of stock (except nonvoting stock which is limited and preferred as to dividends), but only if in both cases such ownership continues until the completion of the intercorporate liquidation.

(d) *Adjustment of equity invested capital.* If property is received by the transferee in an intercorporate liquidation, in computing the equity invested capital of the transferee for any day following the completion of such intercorporate liquidation—

(1) With respect to any share of stock in the transferor having in the hands of the transferee, immediately prior to the receipt of any property in such intercorporate liquidation, a basis determined to be a cost basis, the earnings and profits or deficit in earnings and profits of the transferee shall be computed as if on the day following the completion of such intercorporate liquidation the transferee had realized a recognized gain equal to the amount of the plus adjustment in respect of such share, or had sustained a recognized loss equal to the amount of the minus adjustment in respect of such share;

(2) With respect to any share of stock in the transferor having in the hands of the transferee, immediately prior to the receipt of any property in such intercorporate liquidation, a basis determined to be a basis other than a cost basis, there shall be treated as an amount includible in the sum specified in section 458 (d) the amount of the plus

adjustment with respect to such share, or as an amount includible in the sum specified in section 458 (e) the amount of the minus adjustment with respect to such share.

(e) *Invested capital basis.* The adjusted basis which property received by the transferee in an intercorporate liquidation is considered to have under the provisions of subsection (c) at the time of its receipt shall be thereafter treated as the adjusted basis, in lieu of the adjusted basis otherwise prescribed, in computing any amount, determined by reference to the basis of such property in the hands of the transferee, entering into the computation of the invested capital of the transferee, or of any other corporation the computation of the invested capital of which is determined by reference to the basis of such property in the hands of the transferee.

(f) *Statutory mergers and consolidations.* If a corporation owns stock in another corporation and such corporations are merged or consolidated in a statutory merger or consolidation, then for the purposes of this section and section 458 such stock shall be considered to have been acquired (in such statutory merger or consolidation) by the corporation resulting from the statutory merger or consolidation, and the properties of such other corporation attributable to such stock to have been received by such resulting corporation as a transferee from such other corporation as a transferor in an intercorporate liquidation.

(g) *Determinations*—(1) *Regulations.* Any determination which is required to be made under this section (including determinations in applying this section in cases where there is a series of transferees of the property and cases where the stock of the transferor is acquired by the transferee from another corporation, and the determinations of the basis and adjusted basis which property or items thereof have or are considered to have) shall be made in accordance with regulations which shall be prescribed by the Secretary. If the transferor or the transferee is a foreign corporation, the provisions of this section shall apply to such extent and under such conditions and limitations as may be provided in such regulations.

(2) *Application to liquidation extending over long period.* The Secretary is authorized to prescribe rules similar to those provided in this section with respect to the days within the period beginning with the date on which the first property is received in the intercorporate liquidation and ending with the day of its completion: and the extent to which, and the conditions and limitations under which, such rules are to be applicable.

§ 40.472–1 *Intercorporate liquidation*—(a) *General rule.* For the purposes of section 472, the term "intercorporate liquidation" means the receipt, whether or not after June 30, 1950, by a corporation (hereinafter called the "transferee") of property in complete liquidation of another corporation (hereinafter called the transferor") to which—

(1) The provisions of section 112 (b) (6), or the corresponding provisions of a prior revenue law, are applicable, including the case in which an election has been made pursuant to the last sentence of section 113 (a) (15) of the Revenue Act of 1936, as amended by section 808 of the Revenue Act of 1938, or

(2) A provision of law is applicable prescribing the nonrecognition of gain or loss in whole or in part upon such receipt, including a provision of the regulations applicable to a consolidated return, but not including the provisions of section 112 (b) (7) relating to certain complete liquidations, or the provisions of section 112 (b) (9) relating to certain complete liquidations of railroad corporations, or the provisions of section 112 (b) (10) relating to reorganizations of corporations in certain receivership and bankruptcy proceedings. A liquidation of a member of an affiliated group during a taxable year, which is a consolidated return period, beginning prior to January 1, 1929, is not an intercorporate liquidation for the purposes of section 472, unless some provision of law other than regulations relating to consolidated returns is applicable prescribing the nonrecognition of gain or loss, in whole or in part, upon the liquidation. A liquidation of a member of an affiliated group during a taxable year, which is a consolidated return period, beginning after December 31, 1933, is not an intercorporate liquidation if it comes within the exceptions provided in consolidated returns regulations, such as articles 37 (a) and 38 (c) (3) of Regulations 89, article 37 (a) (1) and (2) of Regulations 97 and 102, § 23.37 (a) (1) and (2) of Regulations 104, and § 33.37 (a) (1) and (2) of Regulations 110.

The rules provided with respect to the sections of the Code mentioned in this section shall also be applicable with respect to corresponding sections of prior revenue laws.

(b) *Exception.* A transaction is an intercorporate liquidation within the meaning of the foregoing provisions only if none of the property received by the transferee is a stock or a security in a corporation, the stock or securities of which are specified in the law applicable to the receipt of such property as stock or securities permitted to be received (or which would be permitted to be received if they were the sole consideration) without the recognition of gain.

Thus, assume that Corporation P owned all the outstanding stock of Corporation S. Pursuant to a plan of reorganization, Corporation S transferred all its assets to Corporation S (1) in exchange for all the capital stock of Corporation S (1), and distributed such stock to Corporation P in liquidation. The entire property received by Corporation P upon the liquidation of Corporation S was stock in a corporation which pursuant to section 112 (b) (3) Corporation P was permitted to receive without the recognition of gain. Consequently, the transaction in which Corporation P acquired the stock of Corporation S (1) in complete liquidation of Corporation S is not an intercorporate liquidation within the provisions of section 472. If the reorganization had occurred in a taxable year beginning prior to January 1, 1934, and the stock of Corporation S (1) had been acquired pursuant to a plan of reorganization by Corporation P without the surrender of the stock of Corporation S, such acquisition by Corporation P of all the assets of Corporation S would not constitute an intercorporate liquidation within the meaning of section 472, since the stock of Corporation S (1) is a stock specified in section 112 (g) of the Revenue Act of 1932 and corresponding provisions of prior revenue laws as stock in a corporation permitted to be received without the recognition of gain. If the stock of Corporation S (1) was acquired by Corporation P in a taxable year beginning subsequent to December 31, 1933, without the surrender or cancellation or retirement of the stock of Corporation S, since the transaction would not be one in which gain or loss is not recognized to Corporation P, the transaction would not be an intercorporate liquidation under section 472. (See § 29.112 (g)–5 of Regulations 111.)

Assume that Corporation P owned the entire outstanding capital stock of Corporation S and that Corporation S owned the entire outstanding capital stock of Corporation S (1). If Corporation P acquired the stock of Corporation S (1) in a complete liquidation of Corporation S pursuant to the provisions of section 112 (b) (6), such liquidation would be an intercorporate liquidation within the provisions of section 472 since section 112 (b) (6) does not specify stock in any corporation as stock permitted to be received without the recognition of gain.

If, in connection with an intercorporate liquidation described in this section, there is also involved (1) the transfer by the transferor to the transferee of property not attributable to the shares of the transferor owned by the transferee in consideration of stock issued by the transferee in an exchange described in section 112 (b) (4) or in an exchange not within the provisions of section 112 (b), or (2) the transfer to the transferee by minority shareholders of the transferor of stock of the transferor in consideration of the issuance by the transferee of stock in an exchange described in section 112 (b) (3) or in an exchange not within the provisions of section 112 (b), the amount includible in the equity invested capital as a result of the receipt of such property or such stock in the exchanges described in (1) or (2) of this sentence shall be determined pursuant to the provisions of section 471 or of section 458 (d) (1) or (2), as the case may be. (See § 40.471–2 and section 458.)

(c) *Statutory merger or consolidation.* In any case in which one corporation owns stock in another corporation (hereinafter called the "transferring corporation"), whether or not such stock ownership amounts to control, and such corporations are merged or consolidated in a statutory merger or consolidation, for the purposes of section 472 and of section 458, the corporation resulting from the statutory merger or consolidation (hereinafter called the "resulting corporation") shall be considered first to have acquired the stock of such transferring corporation in the statutory merger or consolidation and then to have acquired the properties of such transferring corporation which are attributable to the stock considered to have been acquired by the resulting corporation in the statutory merger or consolidation as a transferee from the transferring corporation as a transferor in an intercorporate liquidation. The foregoing rule is equally applicable to all cases of statutory merger and consolidation, whether the resulting corporation operates under the charter of the parent, the subsidiary, or under a new charter.

(d) *Intercorporate liquidation involving foreign corporation.* An exchange which would otherwise be an intercorporate liquidation subject to the provisions of section 472, but which involves a foreign corporation as the transferor or transferee, shall not constitute an intercorporate liquidation for the purposes of section 472 if such exchange was consummated after June 6, 1932, and involved gain unless, prior to such exchange, it was established to the satisfaction of the Commissioner pursuant to the provisions of section 112 (i) and § 29.112 (i)–1 of Regulations 111 or the corresponding provisions of prior revenue laws and regulations, that such exchange was not in pursuance of a plan having as one of its principal purposes the avoidance of Federal income taxes.

§ 40.472–2 *Definition of plus adjustment and minus adjustment.* For the purposes of determining the adjustment of equity invested capital under section 472 (d) and § 40.472–7:

(a) *Plus adjustment.* The term "plus adjustment" means the amount computed with respect to an intercorporate liquidation and determined to be equal to the amount by which the aggregate of the amount of money received by the transferee in the intercorporate liquidation and of the adjusted basis at the time of receipt of all property, other than money, so received exceeds the sum of—

(1) The aggregate of the adjusted basis of each share of stock with respect to which the property was received in the intercorporate liquidation, and

(2) The aggregate of the liabilities of the transferor assumed by the transferee in connection with the receipt of the property in the intercorporate liquidation, of the liabilities (not assumed by the transferee) to which the property so received was subject, and of any other consideration other than the stock with respect to which such property was so received given by the transferee for such property so received.

(b) *Minus adjustment.* The term "minus adjustment" means the amount computed with respect to an intercorporate liquidation and determined to be equal to the amount by which the sum of—

(1) The aggregate of the adjusted basis of each share of stock with respect to which the property was received in the intercorporate liquidation, and

(2) The aggregate of the liabilities of the transferor assumed by the transferee in connection with the receipt of the property in the intercorporate liquidation, of the liabilities (not assumed by the transferee) to which the property so received was subject, and of any other consideration other than the stock with respect to which such property was so received given by the transferee for such property so received,

exceeds the aggregate of the amount of money received by the transferee in the intercorporate liquidation and of the adjusted basis at the time of receipt of all property other than money so received.

(c) *Rules applicable in determining plus adjustment and minus adjustment.* For the purpose of determining the plus adjustment and the minus adjustment provided by section 472 (b):

(1) The adjusted basis of each share of stock with respect to which property is received upon the intercorporate liquidation shall be determined immediately prior to the receipt in the intercorporate liquidation of the property with respect to such share. As to the computation of the adjusted basis of such share, see § 40.472–4.

(2) The adjusted basis of property other than money at the time of receipt of such property shall be determined in accordance with the provisions of section 472 (c) and § 40.472–5 or § 40.472–6. This adjusted basis may be different from the adjusted basis otherwise determined under the provisions of section 113.

(3) A share of stock with respect to which property is received upon an intercorporate liquidation means outstanding stock of the transferor owned by the transferee at the time of such liquidation. Outstanding stock of the transferor shall not include shares of the transferor held by it in its treasury as treasury stock. In the case of a complete liquidation of a transferor under the provisions of section 112 (b) (6), such stock refers only to stock of the transferor owned by the transferee at the time of the receipt of the property.

(4) The plus adjustment or the minus adjustment with respect to each share of stock shall be computed in the manner prescribed in section 472 (b) (1) and (2), except that there shall be brought into account only that part of each item specified in such section which is determined to be attributable to such share. The amount of any consideration (other than the stock of the transferor with respect to which property was received upon the intercorporate liquidation) given by the transferee for the property received upon the intercorporate liquidation shall be prorated with respect to each share of stock (other than stock which is limited and preferred as to assets upon liquidation) upon the basis of the percentage which one share of stock is of the total shares of stock of the transferor owned by the transferee at the time of liquidation (not including stock which is limited and preferred as to assets upon liquidation).

(5) In no event shall there be taken into account any plus adjustment with respect to a share of stock which is limited and preferred as to assets upon liquidation of the transferor in excess of the sum of—

(i) The excess of that portion of the net assets to which such share is entitled upon liquidation of the transferor over the adjusted basis to the transferee of such share at the time of liquidation, and

(ii) The amount of any cumulative dividends in arrears upon such share.

(6) Property received by a transferee in an intercorporate liquidation in exchange for stock of the transferee issued by the transferee to the transferor or to minority shareholders of the transferor, whether or not in an exchange within the provisions of section 112 (b) (4) of the applicable revenue law, is not property received upon an intercorporate liquidation, but is property received upon an exchange under section 471 or property paid in under section 458 (d) (1) or (2). Consequently, other consideration given by the transferee for property received upon the intercorporate liquidation within the provisions of section 472 (b) (1) (B) or section 472 (b) (2) (B) does not include stock of the transferee issued in consideration for property which is received at the time of the intercorporate liquidation but which is received in an exchange under section 471 or which is paid in under section 458 (d) (1) or (2).

(d) *Rules applicable in case intercorporate liquidation extends over period of time.* If any distribution in an intercorporate liquidation occurs in an excess profits tax taxable year ending after June 30, 1950, to which the provisions of section 472 are applicable, and if the liquidation is consummated by a series of distributions covering a period of more than one taxable year, the application of the principles of section 472 in the computation of the equity invested capital of the taxpayer shall, in addition to the requirements set forth in section 472, be subject to the following requirements:

(1) The taxpayer shall file with its return for the first excess profits tax taxable year to which the provisions of section 472 are applicable with respect to the intercorporate liquidation a statement describing the plan pursuant to which the distributions in liquidation have been or will be made and setting forth the period within which the transfer of the property of the transferor to the taxpayer has been or is to be completed.

(2) If the intercorporate liquidation involves a distribution in liquidation pursuant to the provisions of section 112 (b) (6), the taxpayer shall comply with the requirements prescribed by § 29.112 (b) (6)–3 of Regulations 111. The bond required by such section shall also contain provisions unequivocally assuring prompt payment of the excess of income and excess profits taxes (plus penalty, if any, and interest) as computed by the Commissioner without regard to the provisions of section 472 over such taxes computed with regard to such section, regardless of whether such excess may or may not be made the subject of a notice of deficiency under section 272 and regardless of whether it may or may not be assessed.

(3) If the intercorporate liquidation involves a distribution in liquidation other than one pursuant to section 112 (b) (6), in addition to the statement required by subparagraph (1) of this paragraph for each of the taxable years which falls wholly or partly within the period of liquidation, the taxpayer shall, at the time of filing its return, file with the collector for transmittal to the Commissioner a waiver of the statute of limitations on assessment and collection. The waiver shall be executed on such form as may be prescribed by the Commissioner and shall extend the period for assessment of all income and excess profits taxes for such year to a date not earlier than one year after the last date

of the period for assessment of such taxes for the last taxable year in which the transfer of the property of the transferor to the transferee may be completed pursuant to the plan filed by the taxpayer. Such waiver shall also contain such other terms with respect to assessment as may be considered by the Commissioner to be necessary to insure the assessment and collection of the correct tax liability for each year within the period of liquidation. For each of the taxable years which falls wholly or partly within the period of liquidation, the recipient corporation shall file a bond, the amount of which shall be fixed by the Commissioner. The bond shall contain all terms specified by the Commissioner, including provisions unequivocally assuring prompt payment of the excess of the income and excess profits tax (plus penalty, if any, and interest) as computed by the Commissioner without regard to the provisions of section 472 over such taxes computed with regard to such provisions, regardless of whether such excess may or may not be made the subject of a notice of deficiency under section 272 and regardless of whether it may or may not be assessed. Any bond required under this paragraph shall have such surety or sureties as the Commissioner may require. However, see section 1126 of the Revenue Act of 1926, as amended, providing that where a bond is required by law or regulations, in lieu of surety or sureties there may be deposited bonds or notes of the United States. Only surety companies holding certificates of authority from the Secretary as acceptable sureties on Federal bonds will be approved as sureties. The bonds shall be executed in triplicate so that the Commissioner, the taxpayer, and the surety or the depository may each have a copy.

(4) Pending the completion of the liquidation, if there is a compliance with this section and § 40.472–1 with respect to intercorporate liquidations, the equity invested capital of the taxpayer for each day following a distribution in liquidation of the transferor shall be determined under section 472, and the plus adjustment or minus adjustment for each such day shall be computed under section 472 (b) subject to the following rules:

(i) If a distribution in liquidation is in complete cancellation and retirement of any specific share or shares of stock of the transferor, a plus adjustment or a minus adjustment with respect to such share or shares shall be computed at the time such distribution occurred pursuant to the provisions of § 40.472–2 (c), and the money and property received upon the distribution, the liabilities of the transferor assumed at the time of the distribution, the liabilities to which the property received in the distribution was subject, and any other consideration (other than the stock of the transferor with respect to which the distribution was received) shall be taken into account in computing the plus adjustment or minus adjustment with respect to such distribution and shall not be allocated to any prior or subsequent distribution.

(ii) If the distribution in liquidation is not in complete cancellation and retirement of any specific share or shares, but extends ratably over all the outstanding shares of the transferor or over all the outstanding shares of a particular class of stock of the transferor, a plus adjustment or a minus adjustment shall be computed at the time of each distribution in accordance with the provisions of § 40.472–2 (c), and—

(*a*) The distribution shall be considered a distribution with respect to each share (or each share of a particular class) held by the transferee;

(*b*) The adjusted basis of each share for the purposes of computing the plus adjustment or the minus adjustment at the time of any distribution shall bear that ratio to the total adjusted basis of such share computed under § 40.472–4 as the excess of the aggregate of the money and adjusted basis (computed under § 40.472–5) of all property other than money received from the transferor as a distribution over the aggregate of the liabilities of the transferor assumed by the transferee or to which property received from the transferor was subject, bears to the excess of the aggregate of the money and adjusted basis of all property other than money (computed under § 40.472–5) held by the transferor at the time of the first distribution in liquidation over the aggregate of the liabilities of the transferor and liabilities to which the property held by the transferor was subject, at the time of the first distribution in liquidation. In no event, however, shall the portion of the total adjusted basis of a share of stock used in computing the plus adjustment or the minus adjustment under this paragraph exceed an amount which, when added to portions of such basis previously used in computing the plus adjustment or minus adjustment in connection with such intercorporate liquidation, equals the total adjusted basis of such share computed under § 40.472.4;

(*c*) The amount of any consideration (other than the stock of the transferor with respect to which the distribution was received) given by the transferee at the time of the distribution and the amount of any liability of the transferor assumed at the time of the distribution or any liability to which the property received in the distribution was subject shall be taken into account in computing the plus adjustment or the minus adjustment with respect to such distribution, and shall not be allocated to any other prior or subsequent distribution.

(iii) In no event shall the aggregate of the plus adjustments and minus adjustments computed with respect to an intercorporate liquidation extending over a period of time be different for each day after the last day of the last distribution in liquidation than the plus adjustment or minus adjustment which would have resulted had the intercorporate liquidation been commenced and completed entirely during such last day.

§ 40.472–3 *Determination of basis of stock; cost basis or basis other than cost*—(a) *Cost basis.* In all cases other than those in which the basis of stock is determined to be a basis other than cost under paragraphs (b) or (c) of this section, the basis of stock shall be determined to be a cost basis.

(b) *Basis other than cost.* Stock in any corporation shall be determined to have a basis other than cost if, as a result of the transaction in which such stock was acquired—

(1) The basis of such stock is fixed by reference to the basis of other property previously held by the acquiring corporation, not including any case in which the basis of such other property to such corporation was a cost basis if, at the time of the acquisition of such stock or immediately thereafter, the acquiring corporation or its shareholders were in control of the corporation from which such stock was acquired or the corporation from which such stock was acquired or its shareholders were in control of the acquiring corporation; or

(2) The basis of such stock is fixed by reference to its basis in the hands of a preceding owner not including any case in which—

(i) Such stock was acquired from another member of an affiliated group of corporations in a taxable year in which the acquiring corporation and the transferring corporation filed a consolidated return and

(*a*) The basis of such stock to the transferring corporation was a cost basis, or

(*b*) The basis of the stock of the transferring corporation or of any other member of the affiliated group holding stock of the transferring corporation, directly or indirectly, was a cost basis, whether or not the basis to the transferring corporation of the stock transferred was a cost basis (see § 40.472–4 (c) relating to amount of basis) except in those cases in which such stock would have a basis other than cost if it had been acquired in an intercorporate liquidation described in subdivision (ii) of this subparagraph or in an exchange described in subdivision (iii) of this subparagraph; or

(ii) Such stock was acquired in an intercorporate liquidation if immediaitely prior to such liquidation the stock of the liquidated corporation was held by the acquiring corporation with a cost basis (see section 472 (e)), or the stock which was acquired in such liquidation was held by the liquidated corporation with a cost basis; or

(iii) Such stock was acquired from another member of a controlled group of corporations and

(*a*) The basis of such stock to the preceding owner was a cost basis, or

(*b*) The basis of the stock of the transferring corporation or of any other member of the controlled group holding stock of the transferring corporation, directly or indirectly, was a cost basis, whether or not the basis to the transferring corporation of the stock transferred was a cost basis (see § 40.472–4 (c) relating to amount of basis) except in those cases in which such stock would have a basis other than cost if it had been acquired in an intercorporate liquidation described in subdivision (ii) of this subparagraph;

provided that if, in the opinion of the Commissioner, the liquidation of the transferor whose stock was acquired in a transaction subject to the provisions of subdivisions (i) and (iii) of this subparagraph has the effect of a substitution of one member of a controlled group for another member of such group, the provisions of subdivisions (i) and (iii) of this subparagraph shall not be applicable. For the purposes of this section a controlled group includes one or more chains of corporations connected through stock ownership with a common parent corporation if stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of each of the corporations (except the common parent corporation) is owned directly by one or more of the other corporations and the common parent corporation owns directly stock possessing at least 80 percent of the voting power of all classes of stock and at least 80 percent of each class of the nonvoting stock of at least one of the other corporations. As used in the preceding sentence, the term "stock" does not include nonvoting stock which is limited and preferred as to dividends.

(c) *Statutory merger or consolidation.* In any case in which a corporation held stock in another corporation and such corporations were merged or consolidated in a statutory merger or consolidation, such stock, for the purposes of section 472 (f), shall be determined to have a cost basis in the hands of the corporation resulting from the merger or consolidation if such stock was held with a cost basis immediately prior to the statutory merger or consolidation and if, immediately thereafter, the shareholders of the holding corporation were in control of the corporation resulting from the statutory merger or consolidation. In all other cases, such stock shall be determined to have a basis other than cost in the hands of the corporation resulting from the statutory merger or consolidation.

(d) *Control.* For the purposes of this section, in determining whether the basis of stock is a cost basis or a basis other than a cost basis, the term "control" means the ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of the corporation (except nonvoting stock which is limited and preferred as to dividends).

(e) *Series of stock transfers.* The rules provided in this section shall be applicable in determining the basis of stock held by a transferee where there has been a series of transfers of such stock.

§ 40.472–4 *Computation of basis of stock; amount of basis.* The following rules are applicable in determining the adjusted basis of the stock with respect to which the property was received in the intercorporate liquidation, for the purposes of the computation of the plus adjustment or the minus adjustment under section 472 (b):

(a) *Time of computation.* The adjusted basis of each share of stock with respect to which property is received in an intercorporate liquidation shall be determined immediately prior to the receipt of any property in such liquidation with respect to such share. In case of the receipt by a corporation in a statutory merger or consolidation of shares of stock of another corporation, the properties of which are deemed to have been transferred to the acquiring corporation with respect to such stock, the adjusted basis of such stock shall be determined immediately prior to the statutory merger or consolidation.

(b) *Determination of basis.* The adjusted basis of each share of stock shall be the unadjusted basis for determining loss upon a sale or exchange, adjusted by amounts proper under section 115 (*l*) for determining earnings and profits, under the law applicable to the year in which the intercorporate liquidation began. If such stock has a basis fixed by reference to the basis of such stock in the hands of any preceding owner, the basis of such stock to the transferee upon its receipt shall be the basis to the prior owner determined without regard to its value as of March 1, 1913, and adjusted in the hands of the prior owner (and in the hands of any owners prior to such prior owner if the basis of such stock is determined by reference to the basis in the hands of such other prior owners) by an amount equal to the adjustments proper under section 115 (*l*) for determining earnings and profits. In any case in which such stock has a basis to the transferee fixed by reference to the basis of such stock in the hands of any preceding owner, and the basis of such stock in the hands of such preceding owner is different for invested capital purposes, because of the provisions of section 472, then for the purposes of determining gain or loss upon a sale or exchange, the basis of such stock for invested capital purposes, rather than the basis for determining gain or loss upon a sale or exchange, shall be used in determining the unadjusted basis of such stock to the transferee. If the basis of such stock to the preceding owner was a cost basis which is preserved to the transferee, and if the preceding owner was in control of the transferor as defined in section 472 (c) (3), the adjustments prescribed by this section with respect to stock owned by a transferee shall also be made with respect to the stock owned by the preceding owner for the purposes of determining the unadjusted basis of such stock to the transferee.

(c) *Acquisition of stock from member of affiliated or controlled group.* If stock of a corporation was acquired by a member of an affiliated group of corporations from another member of such affiliated group in a transaction subject to the provisions of § 40.472–3 (b) (2) (i) (*b*), or by a member of a controlled group of corporations as defined in § 40.472–3 (b) (2) from another member of such controlled group in a transaction subject to the provisions of § 40.472–3 (b) (2) (iii) (*b*), the basis of such stock to the acquiring corporation shall be an amount equal to the basis which such stock would have, determined pursuant to the provisions of section 472 (c) (1) and (e), if such stock were acquired as the result of an intercorporate liquidation of the corporation transferring such stock and of each member of the group owning stock of the transferring corporation, directly or indirectly, through which such stock would have passed prior to its acquisition by the member of the group.

(d) *Nonapplication of adjustment based on loss during consolidated return period.* If the transferee owns stock of a transferor with which it has made a consolidated return, the basis of such stock shall not be reduced pursuant to the provisions of section 113 (a) (11), or pursuant to a provision of consolidated returns regulations such as § 33.34 (c) of Regulations 110, or § 23.34 (c) of Regulations 104, or corresponding provisions of prior consolidated returns regulations, or similar rules of law applicable to consolidated returns, relating to decrease in basis of stock of a corporation on account of losses sustained by such corporation during a consolidated return period.

(e) *Precontrol distributions in case of cost basis stock.* As of the date of acquisition of control by the transferee (or as of the time of the intercorporate liquidation in case control was not acquired by the transferee), the basis of the aggregate assets of the transferor attributable to stock owned by the transferee with a cost basis is to be revalued to accord with such cost basis. See section 472 (c). Distributions from earnings and profits of the transferor between the date of acquisition of such stock and the date of acquisition of control (or the time of the intercorporate liquidation in case control was not acquired) may have the effect of reducing the assets of the transferor properly subject to revaluation. For the purpose of section 472 in the case of such distributions made with respect to stock having a cost basis, the basis of such stock shall be reduced by an amount proper to give effect to any such reduction in assets.

(f) *Postcontrol distributions in case of cost-basis stock.* If the stock of the transferor is deemed to have a cost basis to the transferee, the adjusted basis of the assets of the transferor must be recomputed pursuant to the provisions of section 472 (c) (1) and § 40.472–5 (a). A subsequent sale or other disposition of the assets of the transferor involved in such recomputation, or the use of such assets in the trade or business of the transferor, will affect the earnings and profits of the transferor in amounts determined by reference to the recomputed basis. In determining whether a distribution made by the transferor to the transferee after the acquisition of control by the transferee of the transferor is a dividend within the meaning of section 115 (a) or a distribution in reduction of the basis of the stock of the

transferor under section 113 (b) (1) (D) for the purposes of the computation of the adjusted basis of such stock to be used in the computation of the plus adjustment or the minus adjustment under section 472 (b), the earnings and profits of the transferor recomputed in accordance with the method prescribed in this subsection shall be used in lieu of the earnings and profits of the transferor otherwise determined.

§ 40.472–5 *Basis of property received in an intercorporate liquidation with respect to stock having a cost basis*—(a) *Determination.* For the purpose of determining the plus adjustment or the minus adjustment to be used in adjusting the equity invested capital of a transferee in an intercorporate liquidation pursuant to section 472 (b) and (d), the property received by a transferee in an intercorporate liquidation attributable to a share of stock of the transferor having in the hands of the transferee a basis determined under § 40.472–3 to be a cost basis shall be considered to have at the time so received an adjusted basis determined as follows:

(1) *Basis of property with respect to stock acquired on or before date of acquisition of control of transferor.* With respect to a share of stock of the transferor acquired by the transferee with a cost basis on or before the date of acquisition by the transferee of control of the transferor, the aggregate of the property (other than money) held by the transferor at the time of the acquisition by the transferee of control of the transferor shall be considered to have an aggregate basis equal to the amount determined by—

(i) Multiplying the amount of the adjusted basis of such share in the hands of the transferee at the time of acquisition of control by the aggregate number of share units in the transferor at such time, the interest represented by such share being taken as the share unit,

(ii) Adding to the amount determined under subdivision (i) of this subparagraph the amount of the liabilities of the transferor at the time of acquisition of control, and

(iii) Subtracting from the sum of the amounts determined under subdivisions (i) and (ii) of this subparagraph the amount of money on hand in the transferor at the time of acquisition of control.

(2) *Basis of property with respect to stock acquired after acquisition of control of transferor.* If a share of stock of the transferor was acquired by the transferee with a cost basis after the transferee acquired control of the transferor, the aggregate basis of the property of the transferor (other than money) held by the transferor at the time of the acquisition by the transferee of such share of the transferor shall be determined in the manner prescribed in subparagraph (1) of this paragraph, except that such computation shall be made as of the time of the acquisition of such share. A share of stock shall be considered to have been acquired after the transferee acquired control of the transferor only if, after the acquisition of such share, the transferee did not lose control of the transferor. A share of stock shall be considered to have been acquired on or before the date of acquisition of control if, after the acquisition of such share, the transferee lost control previously held in the transferor and subsequently reacquired and retained control until the time of the intercorporate liquidation.

(3) *Basis of property with respect to stock in transferor in which control is not acquired.* If a share of stock is owned in a transferor and if immediately prior to the receipt of any property in the intercorporate liquidation in respect of such share the transferee does not have control of the transferor, the aggregate basis of the property of the transferor shall be determined in the manner prescribed in subparagraph (1) of this paragraph, except that such computation shall be made as of the time immediately prior to the receipt of the property in the intercorporate liquidation.

(4) *Redetermination of basis of property to accord with basis of stock.* The amount determined under subparagraphs (1), (2), or (3) of this paragraph, representing the aggregate basis of the property of the transferor at the time of acquisition of control of the transferor, at the time of acquisition of stock of the transferor subsequent to the acquisition of control, or at the time of the intercorporate liquidation may be greater or less than the amount of the aggregate adjusted basis of the property of the transferor at such time otherwise computed. Ordinarily, if—

(i) The aggregate basis of the property of the transferor determined under subparagraph (1), (2), or (3) of this paragraph exceeds the aggregate adjusted basis of such property otherwise computed, such excess shall be deemed to be the basis of an asset which, for the purposes of section 472, shall be called "positive good will," or

(ii) The aggregate basis of the property of the transferor determined under subparagraph (1), (2), or (3) of this paragraph is less than the aggregate adjusted basis of such property otherwise computed, such difference shall be deemed to represent a deduction from the aggregate basis of the property of the transferor otherwise computed; such difference shall be represented in a credit account to be called "negative good will."

If the fair market value of the property of the transferor at the time as of which the recomputation is made is greater or less than the aggregate adjusted basis of such property determined without regard to subparagraph (1), (2), or (3) of this paragraph, proper adjustment shall be made to the basis of such assets to reflect such difference.

(5) *Basis of property acquired by transferor subsequent to determination of basis under (4).* In any case in which the transferor, subsequent to the date as of which the redetermination of the basis of its property has been made pursuant to subparagraph (4) of this paragraph, acquires additional property, the basis of which is fixed by reference to the basis of the property redetermined under subparagraph (4) of this paragraph, the basis of such additional property shall be determined with respect to the basis of such property redetermined in accordance with the rules set forth in subparagraph (4) of this paragraph in lieu of the basis otherwise prescribed with respect to such property.

(6) *Use of basis determined for subsequent adjustments.* The basis of the property determined under subparagraph (4) or (5) of this paragraph shall be used in determining, for the purposes of section 472, all subsequent adjustments to the basis of such property, as, for example, the adjustment based upon depreciation or depletion. Such basis shall also be used in lieu of the basis otherwise prescribed by section 113 in determining, for the purposes of section 472, the gain or loss resulting from a sale or other disposition of such assets by the transferor. The adjustments so obtained and the amount of gain or loss resulting from a sale or other disposition of such assets so determined shall, for the purposes of section 472, be used in computing the earnings and profits or the deficit in earnings and profits of the transferor to ascertain—

(i) Whether distributions subsequent to the date as of which the aggregate basis of the assets of the transferor is determined with respect to stock having a cost basis are out of earnings and profits of the transferor;

(ii) The amount to be included in the earnings and profits of the transferee as a result of such distributions out of earnings and profits of the transferor; or

(iii) The adjustment to be made to the basis of the stock of the transferor owned by the transferee resulting from any such distributions not out of earnings and profits of the transferor.

(7) *Property received by transferee in intercorporate liquidation.* The property received by the transferee in an intercorporate liquidation attributable to a share of stock of the transferor having a cost basis shall be considered to have, at the time of its receipt by the transferee in the intercorporate liquidation, a basis determined as follows:

(i) With respect to property so received which was owned by the transferor with a basis not determined by reference to this paragraph, for example, property the basis of which had not been increased or decreased in a revaluation under subparagraph (4) of this paragraph or property acquired subsequent to the date of such revaluation, such property shall have the same basis to the transferee which it had in the hands of the transferor immediately prior to the intercorporate liquidation, adjusted, however, by adjustments proper under section 115 (l) for the determination of earnings and profits;

(ii) With respect to property so received which was owned by the transferor with a basis increased or decreased as the result of a recomputation pro-

vided by subparagraph (4) of this paragraph, and with respect to property so received which had a basis fixed, as provided by subparagraph (5) of this paragraph, by reference to other property the basis of which was recomputed pursuant to the provisions of subparagraph (4) of this paragraph, such property shall have the same basis to the transferee which it had in the hands of the transferor, so increased or decreased, immediately prior to the intercorporate liquidation adjusted, however, by adjustments proper under section 115 (l) for the determination of earnings and profits; only such part of the aggregate property received by the transferee in the intercorporate liquidation as is attributable to the share of stock with a cost basis shall be considered as having the recomputed basis which such property is deemed to have under subparagraph (4) or (5) of this paragraph.

(b) *Control.* For the purposes of this section, "control" means the ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and the ownership of at least 80 percent of the total number of shares of all other classes of stock (except nonvoting stock which is limited and preferred as to dividends), and shall be determined under the following rules:

(1) Control must be continued until the completion of the intercorporate liquidation.

(2) If control is lost and later reacquired (except as otherwise provided in subparagraph (3) of this paragraph), the date of the last acquisition of control shall be considered to be the date of acquisition of control.

(3) If control, once acquired, was lost because stock of the transferor which did not possess voting power at the time such control was acquired became entitled to vote, and if control was reacquired either because the stock which became entitled to vote lost its voting power or through the acquisition of the requisite portion of such stock, and such control continues until the completion of the intercorporate liquidation, the date of acquisition of control shall be the date upon which control was first acquired.

(4) Except as otherwise provided in subparagraph (6) of this paragraph, if stock of a corporation was acquired from another corporation which had held such stock with a cost basis, and if such stock is determined to have a cost basis in the hands of the acquiring corporation fixed by reference to its basis in the hands of such other corporation, the acquiring corporation shall be deemed to have acquired such stock as of the date upon which such stock was acquired by such other corporation.

(5) If stock of a corporation was acquired from another corporation in a liquidation subject to the provisions of section 112 (b) (6), or the corresponding provisions of a prior revenue law, and if the stock of the liquidated corporation was held by the acquiring corporation with a cost basis but the stock acquired was held by the liquidated corporation with a basis other than cost, the acquiring corporation shall be deemed to have acquired the stock received in the liquidation as of the date upon which it had acquired the stock of the liquidated corporation.

(6) If stock of a corporation was acquired from another corporation in a liquidation subject to the provisions of section 112 (b) (6), or the corresponding provisions of a prior revenue law, and if the stock so acquired was held by the liquidated corporation and the stock of the liquidated corporation was held by the acquiring corporation, both with a cost basis, the acquiring corporation shall be deemed to have acquired the stock received in the liquidation as of the date upon which such stock was acquired by the liquidated corporation, or as of the date upon which the acquiring corporation acquired the stock of the liquidated corporation with respect to which the distribution was made, whichever date was the later.

(7) If stock of a corporation was acquired with a basis determined to be a cost basis under § 40.472–3 (b) (1) because the basis of such stock was fixed by reference to the cost basis of other stock in the hands of the acquiring corporation, the acquiring corporation shall be deemed to have acquired such stock as of the date upon which it had acquired such other stock.

(8) If the basis of the stock of a transferor in the hands of the transferee was increased as the result of a statutory merger or consolidation of the transferor and another corporation, or as the result of a transaction having the effect of a statutory merger or consolidation, and if the stock of such other corporation was held by the transferee with a cost basis, that portion of the transferee's stockholding interest in the transferor represented by the increase shall be deemed to have been acquired as of the date upon which the transferee had acquired the stock of such other corporation.

§ 40.472–6 *Basis of property received in an intercorporate liquidation with respect to stock having a basis other than cost.* For the purpose of determining the plus adjustment or the minus adjustment to be used in adjusting the equity invested capital of a transferee in an intercorporate liquidation pursuant to section 472 (b) and (d), the property received by a transferee in an intercorporate liquidation attributable to a share of stock of the transferor having in the hands of the transferee a basis determined under § 40.472–3 to be a basis other than cost shall be considered to have at the time so received by the transferee the basis it would have had if the first sentence of section 113 (a) (15) had been applicable, i. e., the basis of such property to the transferee shall be the basis which such property had in the hands of the transferor, adjusted by adjustments proper under section 115 (l) in determining earnings and profits. Such basis shall be used for the purposes of section 472 in lieu of the basis for determining gain or loss upon a sale or other disposition prescribed by any provision or rule of law such as the last sentence of section 113 (a) (15), or the corresponding provisions of a prior revenue law, or a provision of consolidated return regulations such as § 33.38 (c) (3) of Regulations 110, or § 23.38 (c) (3) of Regulations 104, or corresponding sections of other consolidated returns regulations. Only such part of the aggregate property of the transferor received by the transferee in the intercorporate liquidation as is attributable to a share having a basis determined to be a basis other than cost shall be considered as having the adjusted basis which property is deemed to have under section 472 (c) (2) and this section. Thus, if the aggregate basis of the assets to the transferor, properly adjusted by the adjustments required by section 115 (l) is $400,000, and if the transferee owns 90 percent of the stock of the transferor half of which was held with a basis other than cost, and receives 90 percent of the aggregate property of the transferor upon the intercorporate liquidation, the aggregate basis of the assets received by the transferee with respect to the shares held with a basis other than cost, for the purposes of section 472, is $180,000 (one-half of 90 percent of $400,000).

§ 40.472–7 *Adjustment of equity invested capital.* If property is received by the transferee in an intercorporate liquidation within the meaning of section 472 (a), the equity invested capital of the transferee for any day following the day in which such intercorporate liquidation is completed shall be computed with the following adjustments:

(a) *Adjustment with respect to stock with cost basis.* With respect to any share of stock in the transferor having in the hands of the transferee, immediately prior to the receipt of the property in the intercorporate liquidation, a basis determined under the provisions of § 40.472–3 to be a cost basis the earnings and profits or the deficit in earnings and profits of the transferee shall be computed as if, on the day following the completion of the intercorporate liquidation, the transferee had realized a recognized gain equal to the amount of the plus adjustment in respect of such share or had sustained a recognized loss equal to the amount of the minus adjustment in respect to such share, computed under the provisions of section 472 (b) and § 40.472–2. No other amount shall be included pursuant to any provision or rule of law in the earnings and profits of the transferee as a result of the intercorporate liquidation with respect to such share.

(b) *Adjustment with respect to stock with basis other than cost.* With respect to any share of stock in the transferor having in the hands of the transferee, immediately prior to the receipt of the property in the intercorporate liquidation, a basis determined under the provisions of § 40.472–3 to be a basis other than cost, there shall be treated as an amount includible in the sum specified in section 458 (d) (relating to equity invested capital) for each day following

the intercorporate liquidation the amount of the plus adjustment computed with respect to such share under section 472 (b) and § 40.472–2 (a), or as an amount includible in the sum specified in section 458 (e) (relating to reduction in equity invested capital) for each day following the intercorporate liquidation the amount of the minus adjustment computed with respect to such share under section 472 (b) and § 40.472–2 (b).

(c) *Illustration.* The provisions of section 472 may be illustrated by the following example:

Assume that Corporation S was organized on December 31, 1928, with an authorized capital stock of $25,000 consisting of 1,000 shares of common stock with a par value of $25 per share. On that date, in a transaction within the provisions of section 112 (b) (5) of the Revenue Act of 1928, Corporation S issued to Corporation P 600 shares of its stock in exchange for a patent which had an adjusted basis to P of $15,000, and 400 shares of its stock to individuals in exchange for property with an adjusted basis to such individuals of $10,000. The basis to P of the 600 shares of stock of S is determined to be a basis other than cost. Section 113 (a) (6) and section 40.472–3 (b) (1). On December 31, 1931, P purchased for $80,000 in cash the remaining 400 shares of the stock of S which it retained until the liquidation of S on December 31, 1936, under section 112 (b) (6) of the Revenue Act of 1936, an intercorporate liquidation. The date of acquisition of control of S by P was December 31, 1931. Section 40.472–5 (b). On December 31, 1928, the patent acquired by S had a remaining life of 15 years; on December 31, 1931, the date of acquisition of control of S by P, the patent had a fair market value of $72,000. As of December 31, 1931, the fair market value of the remaining assets of S was identical with their adjusted basis.

Comparative balance sheets of S as of December 31, 1931, the date of acquisition of control by P, and as of December 31, 1936, the date of liquidation of S, are as follows:

| | | *Dec. 31, 1931* | | *Dec. 31, 1936* |
|---|---|---|---|---|
| Assets: | | | | |
| Cash | | $5,000 | | $35,000 |
| Other current assets | | 60,000 | | 120,000 |
| Fixed assets (less depreciation) | | 30,000 | | 130,000 |
| Patent | $15,000 | | $15,000 | |
| Less: Reserve for amortization | 3,000 | | 8,000 | |
| | | 12,000 | | 7,000 |
| Total assets | | 107,000 | | 292,000 |
| Liabilities and capital: | | | | |
| Current liabilities | | $12,000 | | $22,000 |
| Mortgage on fixed assets | | 15,000 | | 10,000 |
| Capital stock | | 25,000 | | 25,000 |
| Surplus (earnings and profits) | | 55,000 | | 235,000 |
| Total liabilities and capital | | 107,000 | | 292,000 |

The plus adjustment or the minus adjustment to be made to the invested capital of P resulting from the intercorporate liquidation of S is a direct addition to or subtraction from the equity invested capital of P with respect to the stock of S held with a basis other than cost (section 472 (d) (2)); it is deemed to be a recognized gain or loss to P as of the day following the intercorporate liquidation with respect to the stock of S held with a cost basis (section 472 (d) (1)). Moreover, the determination of the basis of property received with respect to stock held with a basis other than cost (section 472 (c) (2)) differs from the determination of such basis with respect to stock held with a cost basis (section 472 (c) (1)). Two separate computations must therefore be made.

(1) *Stock with a basis other than cost.* With respect to the 600 shares of stock of S held by P with a basis other than cost, P is deemed to have received 60 percent $\left(\frac{600}{1000}\right)$ of the assets and to have assumed 60 percent of the liabilities of S, as follows:

| | *Total assets* | | *Assets received* |
|---|---|---|---|
| Cash | $35,000 | | $21,000 |
| Other current assets | 120,000 | | 72,000 |
| Fixed assets (less depreciation) | 130,000 | | 78,000 |
| Patent | $15,000 | $9,000 | |
| Less: Reserve for amortization | 8,000 | 4,800 | |
| | 7,000 | | 4,200 |
| Total | 292,000 | | 175,200 |

| | *Total liabilities* | *Liabilities assumed* |
|---|---|---|
| Current liabilities | $22,000 | $13,200 |
| Mortgage on fixed assets | 10,000 | 6,000 |
| Total | 32,000 | 19,200 |

There is a plus adjustment to the equity invested capital of P in the amount of $141,000, computed as follows:

| | | |
|---|---|---|
| Money received by P | $21,000 | |
| Adjusted basis of all other property received by P | 154,200 | |
| Total assets received | | $175,200 |
| Less: Adjusted basis to P of 600 shares of stock of S | $15,000 | |
| Aggregate liabilities assumed | 19,200 | |
| Total | | 34,200 |
| Plus adjustment | | 141,000 |

(2) *Stock with a cost basis.* With respect to the 400 shares of stock of S held by P with a cost basis, the basis of the aggregate property of S is to be recomputed, as of December 31, 1931, the date of acquisition by P of control of S, to accord with the basis of such stock (section 472 (c) (1) (A)), as follows:

| | | |
|---|---|---|
| Cost basis per share of stock ($80,000 divided by 400) | | $200 |
| Number of share units | | 1,000 |
| Product of cost per share and number of share units | | $200,000 |
| Less: Money | | 5,000 |
| Difference | | 195,000 |
| Add: Liabilities: | | |
| Current liabilities | $12,000 | |
| Mortgage on fixed assets | 15,000 | |
| | | 27,000 |
| Basis of aggregate property other than money | | 222,000 |

The excess of the recomputed basis of the aggregate property of S, other than money, over the adjusted basis of such property prior to the recomputation is $120,000 ($222,000 minus $102,000). The only asset which had a fair market value in excess of its adjusted basis prior to the recomputation is the patent. In the recomputation, the basis of the patent is increased by $60,000 under section 472 (c) (1) (A) to its fair market value of $72,000. The remainder of the excess of the recomputed basis of the aggregate property of S other than money over the adjusted basis of such property prior to the recomputation ($120,000 minus $60,000) becomes the basis of an account entitled "positive good will."

As of December 31, 1931, the adjusted basis and the recomputed basis of the property of S would appear as follows:

| | *Adjusted basis* | | *Recomputed basis* |
|---|---|---|---|
| Assets: | | | |
| Cash | $5,000 | | $5,000 |
| Other current assets | 60,000 | | 60,000 |
| Fixed assets (less depreciation) | 30,000 | | 30,000 |
| Patent | $15,000 | $75,000 | |
| Less: Reserve for amortization | 3,000 | 3,000 | |
| | 12,000 | | 72,000 |
| Positive good will | ------- | | 60,000 |
| | 107,000 | | 227,000 |

Pursuant to section 472 (c) (1) (C), the recomputed basis of the patent is to be used in determining all subsequent adjustments to the basis of such asset. Thus, for each of the five years between December 31, 1931, and December 31, 1936, the date of the intercorporate liquidation, the patent will be amortized at $6,000 per year ($72,000 divided by 12), instead of $1,000 per year ($15,000 divided by 15). The total amount included in the reserve for amortization will be $33,000 ($3,000 plus $30,000) instead of $8,000 ($3,000 plus $5,000). As of December 31, 1936, P is deemed to have received with respect to the 400 shares of stock of S held with a cost basis 40 percent $\left(\frac{400}{1000}\right)$ of the assets of S, including the positive good will account, revalued according to section 472 (c) (1) (A) and (C), and to have assumed 40 percent of the liabilities of S. (Section 472 (c) (1) (E).) The adjusted basis of the property of S as of December 31, 1936, prior to the recomputation and as recomputed, and the portion of the assets deemed to have been received and the liabilities deemed to have been assumed by P, are as follows:

| Assets | Prior to recomputation | | As recomputed | | Assets received | |
|---|---|---|---|---|---|---|
| Cash | | $35,000 | | $35,000 | | $14,000 |
| Other current assets | | 120,000 | | 120,000 | | 48,000 |
| Fixed assets (less depreciation) | | 130,000 | | 130,000 | | 52,000 |
| Patent | $15,000 | | $75,000 | | $30,000 | |
| Less: Reserve for amortization | 8,000 | | 33,000 | | 13,200 | |
| | | 7,000 | | 42,000 | | 16,800 |
| Positive good will | | | | 60,000 | | 24,000 |
| Total | | 292,000 | | 387,000 | | 154,800 |

| Liabilities: | *Total liabilities* | *Liabilities assumed* |
|---|---|---|
| Current liabilities | $22,000 | $8,800 |
| Mortgage on fixed assets | 10,000 | 4,000 |
| Total | 32,000 | 12,800 |

There is a plus adjustment deemed to be a recognized gain to P as of January 1, 1937, in the amount of $62,000, computed as follows:

| | | |
|---|---|---|
| Money received by P | $14,000 | |
| Adjusted basis of all other property received by P | 140,800 | |
| Total assets received | | $154,800 |
| Less: Adjusted basis to P of 400 shares of stock of S | $80,000 | |
| Aggregate liabilities assumed | 12,800 | |
| Total | | 92,800 |
| Plus adjustment | | 62,000 |

The unadjusted basis to P of the property received from S in the intercorporate liquidation is computed as follows:

| | Basis with respect to 600 shares | | Basis with respect to 400 shares | | Total | |
|---|---|---|---|---|---|---|
| Cash | | $21,000 | | $14,000 | | $35,000 |
| Other current assets | | 72,000 | | 48,000 | | 120,000 |
| Fixed assets (less depreciation) | | 78,000 | | 52,000 | | 130,000 |
| Patent | $9,000 | | $30,000 | | $39,000 | |
| Less: Reserve for amortization | 4,800 | | 13,200 | | 18,000 | |
| | | 4,200 | | 16,800 | | 21,000 |
| Positive good will | | | | 24,000 | | 24,000 |
| Total | | 175,200 | | 154,800 | | 330,000 |

For the purpose of computing the earnings and profits and the adjusted basis of the patent received from S in the intercorporate liquidation to be used in the determination of the invested capital of P for each excess profits tax taxable year, the patent would be deemed to have an unadjusted basis to P of $21,000 as of January 1, 1937, and the annual amount of amortization from that date would be $3,000 ($21,000 divided by 7) instead of $1,000, the amount of amortization taken by S.

§ 40.472–8 *Invested capital basis.* For the purpose of computing any amount entering into the computation of the invested capital of the transferee, or of any other corporation the computation of the invested capital of which is determined by reference to the basis of property in the hands of the transferee, the adjusted basis which property received by the transferee in an intercorporate liquidation is deemed to have at the time of its receipt by the transferee, determined under section 472 (c) and § 40.472–5, shall be thereafter treated as the adjusted basis of such property in lieu of any other basis otherwise prescribed. Thus, items of depreciation or depletion or any other items computed by reference to the basis of property received in an intercorporate liquidation, shall, for the purpose of computing the invested capital of the transferee, be determined by reference to the adjusted basis of such property in the hands of the transferee computed under section 472 in lieu of any basis prescribed by section 113 or any other provision or rule of law. Likewise, the adjusted basis of stock or other assets received by the transferee in an intercorporate liquidation shall, for the purpose of determining the ratio of inadmissible assets to total assets under section 440 (b), be the adjusted basis as provided in section 472 (c) in lieu of the basis determined under section 113. So, also, for the purpose of determining the earnings and profits resulting from a sale or other disposition of an asset received in an intercorporate liquidation the adjusted basis of such asset shall be the adjusted basis as provided in section 472 (c).

In pursuance of the Internal Revenue Code, the foregoing regulations are hereby prescribed, applicable only to taxable years ending after June 30, 1950. In order that these regulations may be available for guidance to taxpayers for as long a period as possible prior to March 15, 1951 (the date prescribed for filing returns for taxable years ending before January 1, 1951), it is hereby found to be impracticable to incur the delay which would result from the issuance of these regulations with notice and public procedure thereon under section 4 (a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4 (c) of said act.

[SEAL] FRED S. MARTIN,
*Acting Commissioner of Internal Revenue.*

Approved: March 1, 1951.

THOMAS J. LYNCH,
*Acting Secretary of the Treasury.*

[F. R. Doc. 51–2959; Filed, Mar. 2, 1951; 12:22 p. m.]

# TITLE 10—ATOMIC ENERGY

## Chapter I—Atomic Energy Commission

[Domestic Uranium Program Circular 5, Revised]

### PART 60—DOMESTIC URANIUM PROGRAM

GUARANTEED MINIMUM PRICE FOR URANIUM-BEARING CARNOTITE-TYPE OR ROSCOELITE-TYPE ORES OF COLORADO PLATEAU AREA

Section 60.5 and § 60.5a of Title 10, Code of Federal Regulations, are amended by increasing the prices and premiums to be paid after March 1, 1951, for uranium ores, so that § 60.5 and § 60.5a, as amended, shall read as follows:

§ 60.5 *Guaranteed minimum price for uranium-bearing carnotite-type or roscoelite-type ores of the Colorado Plateau area*—(a) *Guarantee.* To stimulate domestic production of uranium-bearing ores of the Colorado Plateau area, commonly known as carnotite-type or roscoelite-type ores, and in the interest of the common defense and security, the United States Atomic Energy Commission hereby establishes the guaranteed minimum prices specified in § 60.5a effective during the period, March 1, 1951, through March 31, 1958, for the delivery of such ores to the Commission at Monticello, Utah, in accordance with the terms of this section and § 60.5a.

NOTE: In §§ 60.1 and 60.2 (Domestic Uranium Program, Circulars No. 1 and 2), the Commission established guaranteed prices for other domestic uranium-bearing ores, mechanical concentrates, and refined uranium products.

(b) *Effect on §§ 60.3 and 60.3a.* Sections 60.3 and 60.3a, which also apply to carnotite and roscoelite ores, are not revoked by the issuance of this section and § 60.5a and sellers may elect to deliver ore under the provisions of §§ 60.3 and 60.3a rather than under this section and 60.5a, at their option, during the unexpired terms of §§ 60.3 and 60.3a (through April 11, 1951). It is believed, however, that in most cases the provisions of this section and § 60.5a will be more favorable to producers.

(c) *Definitions.* As used in this section and in § 60.5a, the term "buyer" refers to the U. S. Atomic Energy Commission, or its authorized purchasing agent. The term "ore" does not include mill tailings or other mill products. The term "seller" refers to any person offering uranium ores for delivery to the

Commission. Weights are avoirdupois dry weights, unless otherwise specifically provided.

(d) *Deliveries of not to exceed 1,000 tons per year.* To aid small producers, any one seller may deliver without a written contract but otherwise in accordance with this circular up to, but not exceeding, 1,000 short tons (2,000 pounds per ton) of ores during any calendar year.

(e) *Deliveries in excess of 1,000 tons per year.* Sellers desiring to deliver in excess of 1,000 short tons (2,000 pounds per ton) of ores during any calendar year will be required to enter into a contract with the Commission providing for, among other things, a rate of delivery and the total quantity of ore to be delivered.

(f) *Delivery.* Seller, at his own expense, shall deliver and unload all ores at the buyer's depot at Monticello, Utah. Deliveries shall be in lots of not less than 10 short tons (2,000 pounds per ton) unless special arrangements have been agreed upon by buyer, but such lots may be delivered in more than one load. Days and hours during which ore may be delivered will be posted at the depot.

(g) *Weighing, sampling and assaying.* Buyer will bear the cost of weighing, sampling, and assaying. The net weight of each load will be determined by the buyer's weighmaster on scales which will be provided by the buyer at or in the vicinity of the purchase depot and such weight will be accepted as final. A weight ticket will be furnished seller or his representative for each load. Each lot of ores will be sampled promptly by the buyer according to standard practice and such sampling will be accepted as final. Seller or his representative may be present at the sampling at his own expense. The absence of seller or his representative shall be deemed a waiver of this right. Buyer will make moisture determinations according to standard practices in ore sampling. All final samples will be divided into four pulps and distributed as follows: (1) The seller, or his representative, will receive one pulp; (2) the buyer will retain one pulp; (3) the other two pulps will be reserved for possible umpire analysis. The buyer's pulp will be assayed by the buyer. The seller may, if he desires, and at his own expense, have his pulp assayed by an independent assayer. In case of disagreement on assays as to any constituent of the ores, an umpire shall be selected in rotation from a list of umpires approved by the buyer whose assays shall be final if within the limits of the assays of the two parties; if not, the assay which is nearer to that of the umpire shall prevail. The party whose assay is the farther from that of the umpire shall pay the cost of the umpire's assay for the constituent of the ores which is in dispute. In the event that the umpire's assay is equally distant from the assay of each party, costs will be split equally. In case of seller's failure to make or submit assays, buyer's assays shall govern. After sampling, the ores may be placed in process, commingled, or otherwise disposed of by buyer.

(h) *Payment.* Buyer will make payment promptly but payment will not be made until an entire minimum lot of ten short tons (2,000 pounds per ton) has been delivered and accepted, unless special arrangements have been agreed upon by buyer, in which case there may be an extra charge for assaying and sampling. Moisture determinations, analyses and settlement sheets, together with the check in payment, will be mailed to seller.

(i) *Inquiries.* All inquiries concerning the provisions of this section and § 60.5a, offers to deliver ores, or questions about the Commission's domestic uranium program in the Colorado Plateau area should be addressed to:

United States Atomic Energy Commission, Post Office Box 270, Grand Junction, Colorado; Telephone: Grand Junction 3000.

(j) *Licenses.* Arrangements will be made by the Commission for the issuance of licenses, pursuant to the Atomic Energy Act of 1946, covering deliveries of source material to the Commission under this section and § 60.5a.

(k) *Limitation of commitment.* Commitments by the Commission to accept delivery of ores are limited to the provisions of this section and § 60.5a as amended from time to time, or to written contracts between the Commission and sellers. Other commitments purporting to be made by the Commission's field personnel or other agents of the Commission will not bind the Commission unless they are in accord with the provisions of this section and § 60.5a or other official circulars.

§ 60.5a. *Schedule I; minimum prices, specifications, and conditions*—(a) *Prices.* Payment for delivery of the ores will be computed on the following basis:

(1) *Uranium.* (i) Ores assaying less than 0.10 percent: no payment. Any such ores which are delivered to the purchase depot shall, unless otherwise specifically agreed to by buyer, become the property of the buyer as liquidated damages for buyer's expense of weighing, sampling, and assaying, and after sampling may be placed in process, commingled, or otherwise disposed of by buyer. If seller has any question as to the quality of his ore, it is suggested that before shipment and delivery to the purchase depot a representative sample be submitted to the buyer or to one of the umpires for assay at seller's expense. The buyer at its discretion may assay a limited number of samples without charge.

(ii) Ores assaying 0.10 percent $U_3O_8$ and more, as follows:

| $U_3O_8$ assay: | *Payment per pound $U_3O_8$* |
|---|---|
| 0.10 percent | $1.50 |
| 0.11 percent | 1.70 |
| 0.12 percent | 1.90 |
| 0.13 percent | 2.10 |
| 0.14 percent | 2.30 |
| 0.15 percent | 2.50 |
| 0.16 percent | 2.70 |
| 0.17 percent | 2.90 |
| 0.18 percent | 3.10 |
| 0.19 percent | 3.30 |
| 0.20 percent and more | 3.50 |

(iii) Premiums on uranium: $0.75 per pound for each pound of $U_3O_8$ in excess of 4 pounds $U_3O_8$ per short ton (2,000 pounds per ton) of ore and an additional premium of $0.25 per pound for each pound in excess of ten pounds $U_3O_8$ per short ton. Fractional parts of a pound will be paid for on a pro rata basis to the nearest cent.

(2) *Vanadium.* $V_2O_5$ at $0.31 per pound up to, but not exceeding, ten pounds of $V_2O_5$ for each pound of $U_3O_8$ contained in ores. No factor will be included for $V_2O_5$ in excess of ten pounds for each pound of $U_3O_8$, although buyer may, from time to time, publicly announce that, for limited periods by written agreements with individual producers, $V_2O_5$ in excess of ten-to-one will be paid for. Any such announcement will be made by posting a notice to this effect at the Monticello depot and through such other channels as are deemed suitable to achieve maximum dissemination among producers. Excess $V_2O_5$ shall be deemed to be buyer's property.

(3) *Allowances.* (i) A development allowance of $0.50 per pound $U_3O_8$ contained in ores assaying 0.10 percent $U_3O_8$ or more in recognition of the expenditures necessary for maintaining and increasing developed reserves of uranium ores. Fractional parts of a pound will be paid for on a pro rata basis to the nearest cent. Sellers accepting this allowance are deemed to agree to spend such funds for the development or exploration of their properties. Sellers delivering less than 1,000 short tons per calendar year will not be required to submit an accounting record of expenditures for development or exploration pursuant to this agreement but sellers delivering in excess of 1,000 short tons per calendar year will be required, under the terms of their contracts, to submit proof satisfactory to the Commission that funds equivalent to the amount received as development allowance have been spent for development or exploration either during the contract period or within six months thereafter, unless otherwise provided in the contract.

(ii) A haulage allowance of 6¢ per ton mile for transportation of ore paid for under §§ 60.5 and 60.5a from the mine where produced to the purchase depot specified by the Commission, up to a maximum of 100 miles. The haulage distance from the mine to the purchase depot will be determined by the Commission and its decision will be final. Tonnages for purposes of this allowance shall be calculated on the basis of natural weights rather than dry weights.

(4) *Adjustment of assays.* Assays shall be adjusted to the nearest 0.01 percent for purposes of payment.

(b) *Quality and size.* Ores will not be accepted by buyer under §§ 60.5 and 60.5a which, in buyer's judgment:

(1) Contain less than 0.10 percent $U_3O_8$;

(2) Contain more than three parts of lime ($CaCO_3$) to one part of $V_2O_5$, or a total of more than 6 percent lime in the ore;

(3) Contain impurities deleterious to buyer's extraction process or for any other reason are not amenable to it;

(4) Contain lumps in excess of twelve inches in size.

NOTE: The Commission will be interested in discussing arrangements for delivery to it of types of uranium-bearing materials other than those for which guaranteed prices have been established, such as tailings, mill products, and ores of types not acceptable under §§ 60.5 and 60.5a.

(60 Stat. 755–775; 42 U. S. C. 1801–1819. Interpret or apply sec. 5, 60 Stat. 761, 42 U. S. C. 1805)

Effective March 1, 1951 through March 31, 1958.

Dated at Washington, D. C., this 26th day of February 1951.

By order of the Commission.

M. W. BOYER,
*General Manager.*

[F. R. Doc. 51-3190; Filed, Mar. 12, 1951; 8:45 a.m.]

# TITLE 24—HOUSING AND HOUSING CREDIT

## Chapter VIII—Office of Housing Expediter

[Controlled Housing Rent Reg., Amdt. 357]

[Controlled Rooms in Rooming Houses and Other Establishments Rent Reg., Amdt. 352]

PART 825—RENT REGULATIONS UNDER THE HOUSING AND RENT ACT OF 1947, AS AMENDED

LOUISIANA

Amendment 357 to the Controlled Housing Rent Regulation (§§ 825.1 to 825.12) and Amendment 352 to the rent regulation for Controlled Rooms in Rooming Houses and Other Establishments (§§ 825.81 to 825.92). Said regulations are amended in the following respects:

1. Schedule A, Item 129, is amended to read as follows:

| Name of defense-rental area | State | County or counties under rent regulation | Maximum rent date | Effective date of regulation | Date by which registration statement to be filed |
|---|---|---|---|---|---|
| (129) Alexandria-Leesville. | Louisiana | The parishes of Beauregard and Vernon. | Jan. 1, 1941 | July 1, 1942 | Aug. 15, 1942 |

This recontrols the Parishes of Beauregard and Vernon in Louisiana, portions of the Alexandria-Leesville, Louisiana, Defense-Rental Area. Vernon Parish was decontrolled as of June 1, 1947. As of October 31, 1947, in Beauregard Parish, the application of the following regulations was terminated: (a) §§ 825.81 to 825.92 (Rent Regulation for Controlled Rooms in Rooming Houses and Other Establishments) in its entirety, and (b) §§ 825.1 to 825.12 (Controlled Housing Rent Regulation) only with respect to furnished rooms, not constituting an apartment, located within the residence occupied by the landlord or his immediate family. As of October 30, 1948, Beauregard Parish was entirely decontrolled.

2. A new Item is hereby incorporated in Schedule B to read as follows:

81. Provisions relating to the Parishes of Beauregard and Vernon, Louisiana, portions of the Alexandria-Leesville, Louisiana, Defense-Rental Area.

*Recontrol of the Parishes of Beauregard and Vernon, Louisiana, portions of the Alexandria-Leesville, Louisiana, Defense-Rental Area.* Effective March 8, 1951, the provisions of §§ 825.1 to 825.12 and 825.81 to 825.92 shall apply to housing accommodations in the Parishes of Beauregard and Vernon, Louisiana, portions of the Alexandria-Leesville, Louisiana, Defense-Rental Area, except as modified by the following provisions:

a. As to housing accommodations in the Parish of Vernon, Louisiana, all orders in effect on May 31, 1947, in accordance with §§ 825.1 to 825.12 or 825.81 to 825.92, shall be in full force and effect.

b. As to housing accommodations in the Parish of Beauregard, the following orders shall be in full force and effect: (i) all orders in effect on October 30, 1947, in accordance with §§ 825.81 to 825.92; (ii) all orders in effect on October 30, 1947, with respect to furnished rooms not constituting an apartment located within the residence occupied by the landlord or his immediate family in accordance with §§ 825.1 to 825.12; (iii) all orders in effect on October 29, 1948, in accordance with §§ 825.1 to 825.12.

c. If, on March 8, 1951, there was a ground for adjustment under § 825.5 (a) or § 825.85 (a) for which no order had previously been issued, and a petition for adjustment is filed on or before April 8, 1951, the adjustment shall be effective as of March 8, 1951.

d. If, on March 8, 1951, the services provided with any housing accommodations are less than the minimum required by § 825.3 or § 825.83, the landlord shall either restore and maintain such minimum services or file a petition on or before April 8, 1951 requesting approval of the decreased services. If, on March 8, 1951, the furniture, furnishings or equipment provided with any housing accommodations are less than the minimum required by § 825.3 or § 825.83, the landlord shall file, on or before April 8, 1951, a written report showing the decrease in furniture, furnishings or equipment. Except as modified by this paragraph "d", the provisions of §§ 825.5 (b) and 825.85 (b) shall be applicable to all such cases.

e. In the case of any action which on March 8, 1951, was required or authorized by §§ 825.1 to 825.12 or 825.81 to 825.92 to be taken within a specified period of time, the same time period shall be applicable but such time period shall be counted from March 8, 1951.

f. The provisions of §§ 825.6 and 825.86 shall not apply to any case in which judgment was entered prior to March 8, 1951 by a court of competent jurisdiction for the eviction or removal of a tenant from housing accommodations.

(Sec. 204, 61 Stat. 197, as amended; U. S. C. App. Sup. 1894)

This amendment shall become effective March 8, 1951.

Issued this 8th day of March 1951.

TIGHE E. WOODS,
*Housing Expediter.*

[F. R. Doc. 51-3230 Filed, Mar. 12, 1951; 8:55 a. m.]

# TITLE 32A—NATIONAL DEFENSE, APPENDIX

## Chapter I—Office of Defense Mobilization

[Defense Mobilization Order 7]

DMO 7—CREATION OF A COMMITTEE ON DEFENSE TRANSPORTATION AND STORAGE

By virtue of the authority vested in me by Executive Order No. 10193 of December 16, 1950, and in accordance with Executive Order No. 10219 of February 28, 1951, and in order to assist the Director of Defense Mobilization to improve the coordination and effectiveness of Federal policies and programs relating to transportation and storage, *It is hereby ordered:*

SECTION 1. There is established in the Office of Defense Mobilization the Committee on Defense Transportation and Storage, which shall consist of a Chairman and one representative each, designated by the Secretaries of State, Treasury, Defense, Interior, and Commerce, the Defense Production Administrator, and the Defense Transport Administrator, respectively, and such other members as the Director of Defense Mobilization may hereafter provide. The Chairman of the Committee shall be designated by the Director of Defense Mobilization.

SEC. 2. The Defense Transportation Committee shall:

(a) Advise the Director of Defense Mobilization on problems relating to defense transportation and storage.

(b) Review Federal policies, plans, and programs relating to defense transportation and storage, and advise the Director of Defense Mobilization concerning policies, methods, and measures for improving the coordination and obtaining the most effective utilization of the various forms and facilities of transportation and storage, including among other matters policies, methods, and measures for the coordination of inland and ocean transportation and the operation of ports.

(c) Review for the Director of Defense Mobilization such proposed legislation, Executive Orders, and administrative orders and regulations relating to transportation and storage as he may direct.

SEC. 3. In carrying out the responsibilities set forth in this order the Committee on Defense Transportation and Storage shall concern itself primarily with interagency problems, policies, and programs relating to defense transportation and storage and with matters relating to two or more forms of transportation under the jurisdiction of different departments or agencies.

(E. O. 10193, Dec. 16, 1950, 15 F. R. 9031, 3 CFR, 1950 Supp.)

This order shall take effect on March 13, 1951.

OFFICE OF DEFENSE MOBILIZATION,
C. E. WILSON,
*Director.*

[F. R. Doc. 51-3271; Filed, Mar. 9, 1951, 4:15 p. m.]

## Chapter III—Office of Price Stabilization, Economic Stabilization Agency

[Administrative Order 22]

AO 22—DELEGATION OF AUTHORITY WITH RESPECT TO ENFORCEMENT FUNCTIONS

By virtue of the authority vested in me as the Director of Price Stabilization pursuant to Executive Order No. 10161 (15 F. R. 6105), Economic Stabilization Agency General Order No. 2 (16 F. R. 738), and Economic Stabilization Agency General Order No. 5 (16 F. R. 1273), and in order to further define the internal organization of the Office of Price Stabilization, particularly the duties, powers, and authority of the Assistant Director of Price Stabilization for Enforcement (Director of Enforcement), *It is hereby ordered:*

SECTION 1. Those functions relating to the enforcement of price stabilization which were delegated to the Director of Price Stabilization by Economic Stabilization Order No. 2 (16 F. R. 738), are hereby redelegated to the Assistant Director of Price Stabilization for Enforcement (Director of Enforcement), who shall have the authority to make and authorize successive redelegations.

SEC. 2. All functions delegated pursuant to this order shall be performed by the Assistant Director of Price Stabilization for Enforcement (Director of Enforcement) subject to such general supervision, direction and control as the Director of Price Stabilization deems expedient.

This order shall become effective March 12, 1951.

Issued this 12th day of March 1951.

MICHAEL V. DISALLE,
*Director of Price Stabilization.*

[F. R. Doc. 51-3334; Filed, Mar. 12, 1951; 11:41 a. m.]

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[General Ceiling Price Regulation, Supplementary Regulation 11]

GCPR, SR 11—MANUFACTURERS' AND WHOLESALERS' PRICES FOR SOFT SURFACE FLOOR COVERINGS

Pursuant to the Defense Production Act of 1950 (Pub. Law 774, 81st Cong.), Executive Order 10161 (15 F. R. 6105), and Economic Stabilization Agency General Order No. 2 (16 F. R. 738), this Supplementary Regulation No. 11 to the General Ceiling Price Regulation (16 F. R. 808) is hereby issued.

STATEMENT OF CONSIDERATIONS

The General Ceiling Price Regulation froze the ceiling price of manufacturers of soft surface floor coverings at their January 26, 1951, level of prices. With respect to most carpets and rugs, wool constitutes half the cost of the finished product. Carpet wool is entirely an imported raw material and has not been brough under control. As a result of steadily increasing wool prices, carpet manufacturers are suffering a squeeze. This supplementary regulation relieves them of most of this squeeze.

The weighted monthly average cost of scoured wool per pound for a representative group of manufacturers, representing approximately 80 percent of the industry during two months of 1950 and the first five months of 1951, is as follows:

| | |
|---|---|
| November 1950 | $1.05 |
| December | 1.13 |
| January 1951 | 1.39 |
| February | 1.76 |
| March | 1.91 |
| April | 2.03 |
| May (3 companies) | 2.11 |

The wool floor covering industry consists of approximately 30 manufacturers, all of whom sell from published price lists. In measuring the amount of price adjustment needed, reference was first made to the prices in effect at the end of June 1950 and beginning of July 1950. These prices were announced prior to June 25 and thus reflected manufacturing costs in existence prior to the outbreak of the Korean hostilities.

On the basis of data gathered from a representative group of manufacturers, increases in direct cost of cotton, jute, and rayon were calculated up to December 31, 1950. The price adjustment granted gives the manufacturers the benefit of such increases in direct costs. In addition, it gives them the benefit of increases in wool prices and direct labor costs up to the present time.

The price relief granted is expressed in the form of a 15 percent increase in the prices which were in effect between December 19, 1950, and January 15, 1951, pursuant to published price lists. Between June 1950 and January 15, 1951, the industry as a whole made several price increases which reflected in part the increased cost of wool. Virtually the entire industry published new lists between December 19, 1950, and January 15, 1951. This period, then, represents the last period in which fairly uniform prices prevailed. A few manufacturers published lists subsequently to January 15, 1951. Had the permitted increase been added to the ceiling prices in effect during the base period for the General Ceiling Price Regulation, December 19, 1950, to January 26, 1951, these manufacturers would have received an unjustified amount.

Retailers apply their mark-up only on the original price without the permitted increase. The amount of the permitted increase is then added to the price which the retailer arrives at. In this fashion the retailer obtains the same dollar margin that he previously enjoyed.

Most floor coverings are sold direct from manufacturers to retailers. Some manufacturers, however, use wholesale distributors. The uniform practice in the industry has been that the wholesalers sell at the same price as the manufacturers and that their mark-up is determined by a percentage discount from the list price. This discount is usually 12 to 14 percent.

The wholesaler performs a somewhat less complete function that in other fields. Usually he is guaranteed against overstocking and losses through obsolescence. The price structure of the industry would make it difficult to provide any absorption by the wholesaler which would benefit the retailer or consumer. In the light of this fact and the relatively small margin which the wholesaler receives, no provisions have been made in this temporary regulation for any absorption by the wholesaler of any part of the increase. The supplementary regulation, therefore, retains the customary discount to wholesalers.

The supplementary regulation provides interim relief. It is expected that a permanent regulation will be issued in due course which will deal more completely with the problems of the industry. In connection with the issuance of a permanent regulation the possibilities of absorption at both the wholesale and retail level will be given further study.

In the judgment of the Director of Price Stabilization, the provisions of the supplementary regulation are generally fair and equitable and are necessary to effectuate the purposes of Title IV of the Defense Production Act of 1950.

So far as practicable the Director of Price Stabilization gave due consideration to the national effort to achieve maximum production in furtherance of the objectives of the Defense Production Act of 1950; to prices prevailing during the period from May 24, 1950, to June 24, 1950, inclusive; and to relevant factors of general applicability.

REGULATORY PROVISIONS

Sec.
1. Applicability of supplementary regulation.
2. Ceiling prices for sales to persons other than wholesalers.
3. Ceiling prices for sales to wholesalers.
4. Ceiling prices for new articles.
5. Notification to retailers.
6. Miscellaneous.

AUTHORITY: Sections 1 to 6 issued under sec. 704, Pub. Law 774, 81st Cong. Interpret or apply Title IV, Pub. Law 774, 81st Cong.; E. O. 10161, Sept. 9, 1950, 15 F. R. 6105.

SECTION 1. *Applicability of supplementary regulation.* This supplementary regulation establishes new ceiling prices for sales by manufacturers and wholesalers of soft surface floor coverings with pile fabrics of wool, synthetic materials, or a blend of both. These ceiling prices supersede the ceiling prices under the General Ceiling Price Regulation.

SEC. 2. *Ceiling prices for sales to persons other than wholesalers.* The ceiling price for any unit of floor covering covered by this order shall be 115 percent of list prices for the same unit of floor covering which was contained in the applicable manufacturer's price list in effect for deliveries at any time between December 19, 1950, and January 15, 1951.

SEC. 3. *Ceiling prices for sales to wholesalers.* Ceiling prices for all sales by manufacturers to wholesalers shall be the ceiling prices established in section 2, less discounts of a percentage no smaller than the discounts in effect during the period from December 19, 1950, to January 26, 1951.

SEC. 4. *Ceiling prices for new articles.* Ceiling prices for new units of floor covering not included in manufacturers' price lists in effect between December 19,

1950, and January 15, 1951, shall be established under the provisions of sections 4 and 5 of the General Ceiling Price Regulation for manufacturers and wholesalers, respectively. In applying these sections, the ceiling prices for a "comparison commodity" shall be the applicable ceiling prices fixed under section 2 or 3 of this supplementary regulation.

SEC. 5. *Notification to retailers.* Each manufacturer or wholesaler must break down his invoice price for each unit sold into two component parts:

The "original price", i. e. the price list price in effect between December 19, 1950 and January 15, 1951 and the "permitted increase", i. e. the amount of any increase above the "original price" permitted by this supplementary regulation. To each invoice shall be affixed by rubber stamp or otherwise the following statement:

The amount on this invoice shown as the "original price" is the cost on which you apply your mark-up under OPS Ceiling Price Regulation 7. The amount shown as "permitted increase" may be added to your price after applying your mark-up. The total becomes your ceiling price.

SEC. 6. *Miscellaneous.* All other provisions of the General Ceiling Price Regulation, not inconsistent with the provisions of this supplementary regulation, shall remain in effect.

*Effective date.* This supplementary regulation to the General Ceiling Price Regulation shall become effective March 13, 1951.

MICHAEL V. DISALLE,
*Director of Price Stabilization.*

MARCH 9, 1951.

[F. R. Doc. 51-3335; Filed, Mar. 12, 1951; 11:41 a. m.]

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## Chapter VI—National Production Authority, Department of Commerce

[NPA Order M-7, as Amended Mar. 9, 1951]

### M-7—ALUMINUM FOR CIVILIAN USE

This order as amended is found necessary and appropriate to promote the national defense and is issued pursuant to the Defense Production Act of 1950. In the formulation of this order, there has been consultation with industry representatives, including trade association representatives, and consideration has been given to their recommendation.

This amendment affects NPA Order M-7 as amended Feb. 21, 1951, as follows: Two items in the list of products in section 3 have been changed, a new paragraph (c) has been added to section 5, and section 6 has been revised to read as set forth below. NPA Order M-7 as amended (including Directions 1, 2, and 3, appearing herein as sections 21, 22, and 23) reads as follows:

Sec.
1. Purpose and scope.
2. Definitions.
3. Aluminum forms and products to which this order applies.
4. Application of order.
5. Use of aluminum.
6. Prohibited use of aluminum.
7. Maintenance, repair, and operating supplies.
8. Exceptions.
9. Inventories.
10. Applications for adjustment.
11. Records and reports.
12. Communications.
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*Directions*

21. Base period: applications for adjustment; December 1950 use.
22. Base period: applications for adjustment; use during first calendar quarter of 1951.
23. Application for adjustment—component parts.

AUTHORITY: Sections 1 to 23 issued under sec. 704, Pub. Law 774, 81st Cong. Interpret or apply sec. 101, Pub. Law 774, 81st Cong.; sec. 101, E. O. 10161, Sept. 9, 1950, 15 F. R. 6105, 3 CFR, 1950 Supp., sec. 2, E. O. 10200, Jan. 3, 1951, 16 F. R. 61.

SECTION 1. *Purpose and scope.* The purpose of this order is to describe how the aluminum remaining after allowing for the requirements of national defense may be distributed and used in the civilian economy. It is the policy of the National Production Authority that aluminum and articles made of aluminum, not required to fill rated orders, shall be distributed equitably through normal channels of distribution, and that due regard shall be given by suppliers to the needs of new and small business.

SEC. 2. *Definitions.* As used in this order:

(a) "Person" means any individual, corporation, partnership, association or any other organized group of persons and includes any agency of the United States or any other government.

(b) "Base period" means the 6 months' period ending June 30, 1950.

(c) "Manufacture" means to put into process, machine, fabricate, or otherwise alter materials by physical or chemical means: *Provided, however,* That as applied to "Castings (foundry products as shipped by the producer)" specified in section 3 the word "manufacture" will also mean the assembly of said items into components or end products.

(d) "Maintenance" means the minimum upkeep necessary to continue a building, machine, piece of equipment or facility in sound working condition, and "repair" means the restoration of a building, machine, piece of equipment or facility to sound working condition when the same has been rendered unsafe or unfit for service by wear and tear, damage, failure of parts or the like: *Provided, however,* Neither maintenance nor repair includes the improvement of any such item with material of a better kind, quality or design.

(e) "Operating supplies" means any aluminum forms or products listed in section 3 which are normally carried by a person as operating supplies according to established accounting practice and are not included in his finished product, except that materials included in such product which are normally chargeable to operating expense may be treated as operating supplies.

SEC. 3. *Aluminum forms and products to which this order applies.* The word "aluminum" as used in this order means only the following aluminum forms and products:

Rod and bar.
Wire (under ⅜").
Cables (electrical transmission only).
Rivets.
Forgings and pressings (before machining).
Impact extrusions.
Castings (foundry products as shipped by the producer).
Rolled structural shapes (angles, channels, zees, tees, etc.).
Extruded shapes.
Sheet (coiled and flat), plate, circles and blanks.
Slugs.
Plain coil foil.
Tubing (extruded, drawn and roll formed).
Tube blooms.
Powder (including atomized, flake, paste and pigments).
Ingot, pig, billets, slabs, granulated.
Purchased scrap.

SEC. 4. *Application of order.* Subject to the exemptions stated in section 8, this order applies to all persons who use any aluminum for purposes of manufacture or construction, or for maintenance, repair, or operating supplies. It does not apply to persons (a) who produce aluminum in or convert it to the forms and products listed in section 3; or (b) who use aluminum in the production of other metals (including aluminized steel), or of metal alloys, the chief constituent of which is not aluminum, or of chemical salts of aluminum and compositions of aluminum used as a catalyst.

SEC. 5. *Use of aluminum.* Subject to the exemptions stated in section 8, and unless specifically directed by the National Production Authority, no person shall use in manufacture or construction:

(a) During December 1950, a quantity by weight of aluminum in excess of 100 percent of his average monthly use of aluminum during the base period.

(b) During the following months a total quantity by weight of aluminum in excess of the percentages specified with respect to each month of his average monthly use of aluminum during the base period:

| | *Percent* |
|---|---|
| January, 1951 | 80 |
| February, 1951 | 75 |
| March, 1951 | 65 |

(c) During the calendar quarter commencing on April 1, 1951, a total quantity by weight of aluminum in excess of 65 percent of his average quarterly use of aluminum during the base period: *Provided, however,* That such use in any one month shall not exceed 40 percent of the permitted quarterly use.

SEC. 6. *Prohibited uses of aluminum.* (a) Commencing on April 1, 1951, no person shall use aluminum, or any component part made therefrom, in the manufacture or assembly of any item included in attached List A, except as permitted therein; and no person shall use in the manufacture or assembly of any item, whether or not included in List A, or any component part therefor, a greater quantity or better grade of aluminum than is necessary for functional or operational purposes, or use aluminum solely for decorative or orna-

mental purposes. However, these prohibitions shall not apply to the use of: (1) aluminum, or component parts made therefrom, on and after April 1, 1951, if such materials were contained in such person's inventory on said date and are wholly unsuitable for use in the manufacture or assembly by such person of any item not included in List A; or (2) any such materials covered by an order placed with a producer and included in such producer's schedule for the first calendar quarter of 1951 which is delivered to such person at his plant prior to May 1, 1951, to the extent that such materials are wholly unsuitable for use in the manufacture or assembly by such person of any item not included in List A. Every person who relies on the exceptions contained in the next preceding sentence shall prepare a detailed record showing: (1) the quantities of aluminum, and component parts made therefrom, which were contained in his inventory on the first days of January, February, March and April 1951, and which were wholly unsuitable for use in his manufacture or assembly of any item not included in List A; and (2) the quantities of such materials wholly unsuitable for such use which were delivered to him on or after April 1, 1951, the names and addresses of the suppliers thereof, and the dates of the orders and acceptances covering such materials together with the applicable mill schedule. Such record shall be retained for at least 2 years and shall be made available at the usual place of business where maintained for inspection and audit by duly authorized representatives of the National Production Authority.

(b) During March 1951, no person shall use in the manufacture or assembly of the items included in attached List A a total quantity by weight of aluminum, or of any component parts made therefrom, in excess of 65 percent of his average monthly use of such materials for such purposes during the base period. To the extent that manufacture or assembly of the items on List A is permitted on or after April 1, 1951, under paragraph (a) of this section, the limitations of section 5 shall apply during April and succeeding months.

(c) Commencing on July 1, 1951, no person shall use aluminum in the manufacture or assembly of any item in attached List B: *Provided, however,* That any such item may be completed if it was in process of manufacture or assembly on or before April 30, 1951, and such completion is effected not later than June 30, 1951: *And provided further,* That windows of the non-residential type may be completed *on or before June 30, 1951,* regardless of when manufacture or assembly is commenced if orders therefor were received by the manufacturer prior to February 20, 1951. During each of the months of March, April, May, and June, 1951, no person may use in the manufacture or assembly of ducts and windows of residential type included in the attached List B a total quantity by weight of aluminum in excess of 65 percent of his average monthly use of aluminum in the manufacture or assembly of such items during the base period.

(d) No person may use in construction any aluminum for any item included in attached List A after May 31, 1951, or for any item contained in attached List B after June 30, 1951: *Provided, however,* That this prohibition will not apply to such use of aluminum for any such item if it was manufactured within the time limits specified in this section.

(e) The prohibitions of this section apply notwithstanding the provisions of NPA Reg. 2 with respect to the filling of rated orders and are not affected by any of the exemptions stated in section 8.

SEC. 7. *Maintenance, repair, and operating supplies.* Unless specifically directed by the National Production Authority, during the 6 months' period commencing on December 1, 1950, and each 6 months' period thereafter, no person shall use for maintenance, repair, and operating supplies a quantity by weight of aluminum in excess of the quantity of aluminum that he used for such purposes during the base period.

SEC. 8. *Exemptions.* (a) The use of aluminum required by any person to fill an order that is rated under the priorities system established by NPA Reg. 2 (15 F. R. 6911, 7185), or to meet any other mandatory order of the National Production Authority, is permitted in addition to the use of aluminum authorized by the provisions of sections 5 or 7.

(b) Pending development of requirements for aluminum conductor (including transmission cable, wire, and bus bar) for the production, transmission, or distribution of electric energy, this order does not presently restrict the use of aluminum conductor, conductor accessories or pole hardware for such purposes, if these items are on hand or the suppliers have accepted orders for these items prior to November 13, 1950, for delivery prior to April 1, 1951. The use of other shapes and forms of aluminum listed in section 3 for the production, transmission, or distribution of electric energy remain subject to the restrictions of this order.

(c) The provisions of sections 5 and 7 do not apply to persons who use less than 1,000 pounds of aluminum during any period of twelve consecutive months: *Provided, however,* That persons who by reason of the provisions of section 5 would be permitted to use less than 1,000 pounds during any period of twelve consecutive months may use during such period a quantity up to 1,000 pounds.

(d) Commencing on February 1, 1951, the provisions of section 5 will not apply to the use of aluminum in the manufacture of collapsible tubes as defined in NPA Order M–27.

SEC. 9. *Inventories.* In addition to the provisions of NPA Reg. 1 (15 F. R. 6253), relating to Inventory Control, it is considered that a more exact requirement applying to users of aluminum is necessary. No person obtaining aluminum for use in manufacture or construction, or for maintenance, repair, or operating supplies, may receive or accept delivery of a quantity of aluminum if his inventory is, or by such receipt would become, in excess of that necessary to meet his deliveries or supply his services on the basis of his scheduled method and rate of operation pursuant to this order during the succeeding 60-day period, or in excess of a "practicable minimum working inventory" (as defined in NPA Reg. 1), whichever is less. For the purpose of this section, aluminum shapes and forms listed in section 3 in which only minor changes or alterations have been effected shall be included in inventory. NPA Reg. 1 will apply to aluminum except as modified by this section.

SEC. 10. *Application for adjustment.* Any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue and exceptional hardship upon him not suffered generally by others in the same trade or industry or its enforcement against him would not be in the interest of the national defense or in the public interest. Each request shall be in writing and shall set forth all pertinent facts and the nature of the relief sought, and shall state the justification therefor.

SEC. 11. *Records and reports.* (a) Persons subject to this order shall preserve the records which they have maintained and will maintain of inventories, receipts, deliveries, and uses of aluminum forms and products commencing with January 1, 1950.

(b) Persons subject to this order shall make records and submit such reports to the National Production Authority as it shall require, subject to the terms of the Federal Reports Act (P. L. 831, 77th Cong., 5 U. S. C. 139–139–F).

SEC. 12. *Communications.* All communications concerning this order shall be addressed to the National Production Authority, Washington 25, D. C., Ref.: M–7.

SEC. 13. *Violations.* Any person who wilfully violates any provisions of this order or any other order or regulation of the National Production Authority or wilfully conceals a material fact or furnishes false information in the course of operation under this order is guilty of a crime and upon conviction may be punished by fine or imprisonment or both. In addition, administrative action may be taken against any such person to suspend his privilege of making or receiving further deliveries of materials or using facilities under priority or allocation control and to deprive him of further priorities assistance.

NOTE: All reporting requirements of this order have been approved by the Bureau of the Budget in accordance with the Federal Reports Act of 1942.

This order, as amended, shall take effect, except as otherwise specifically stated, on March 9, 1951.

NATIONAL PRODUCTION AUTHORITY,
[SEAL] MANLY FLEISCHMANN,
*Administrator.*

LIST A

(See section 6)

The use of the forms and products of aluminum defined in section 3 in the items listed below (excluding repair parts) is subject to the prohibitions stated in this order, except as otherwise stated in this order or the list:

Airfoil (tubing) for windmills
Aluminum wool
Andirons, screens, and fireplace fixtures
Animal cages
Animal training equipment
Animal traps
Applicators for moistening envelopes
Arbors and trellises
Architectural and other building ornamentation
Ash trays
Automobile hardware and trim (except functional parts)
Awnings
Badges
Balloon molds
Bar rails
Barber chairs
Batons
Bathtubs
Beauty parlor equipment
Beer equipment: all items
Bells
Beverage mixing and serving equipment, such as bottle coolers, cocktail shakers, ice buckets and pails, ice chippers and shavers
Bicycles
Bird and pet cages, houses, aquariums, accessories and equipment
Blackboard frames and chalk troughs
Boards: shampoo, tanning
Book covers
Book stacks
Boxes, including match, cigarette, typewriter ribbon
Brackets: light, shelf and wall
Brooms and brushes (except industrial)
Buckles, all types
Buckets, household
Burglar alarms
Burial vaults and urns
Buttons (except for work clothing where necessary to resist corrosion).
Cabinets: kitchen, medicine and radiator
Calendars, calendar pads and parts
Cameras, amateur box type still picture, fixed focus (except reflex)
Candle molds
Canes
Canopies
Cans, including ignition coil and motion picture humidor.
Caps: chimney and vent flue
Card tables
Cards, greeting
Carriages: baby, luggage, strollers, scooters (except functional parts)
Cases:
  Cigar
  Film
  Radio, home type
  Soft drink
  Spectacle
  Vanity
Caskets, and accessory devices
Caster cups, wheel casters and glides
Chicken crates
Chutes: coal, package and waste
Cigarette lighters
Cleaning accessories, such as carpet sweepers, dust pans and scrubbing sets
Clothespins
Coasters
Combs
Containers, foil lined, shoe polish
Coops, brooder, chicken, quail, etc.
Copings
Cornices
Crayon molds
Cups
Curtain, drapery, and carpet hardware
Cutlery handles
Cuspidors
Desk pads
Dispensers, fixed or portable, for soap, lotion, paper, straws, etc.
Dolls
Domestic laundry accessories, such as tubs and boilers, washboards, drain board and tub covers, clothes hampers, ironing boards and tables, garment stretchers and dryers, clothes drying frames, and clothes line hardware
Door chimes
Doors, including, but not limited to:
  Coal
  Door frames
  Dumbwaiter
  Incinerator
  Screen
  Storm
Draperies
Dresser sets
Emblems, medals (except religious), crestings and plates
Fences, wire
Flag poles, stanchions and sockets
Floor scrubbers
Flower boxes, stands and pot holders
Forms, concrete vault casting, wax
Fountains
Frames:
  electric sign
  level
  picture
Frames, Window Screen
Frozen fruit sticks
Furniture
Furniture, hardware (except functional parts)
Games
Garden tools and equipment
Garment hooks, brackets, racks, rods, trees and hangers
Giftware
Gutters, leaders and downspouts.
Hair curlers
Hand-tool handles
Hedge clipping machine
Highway markers, signals and signs
Holders:
  Brush
  Pen
  Soda fountain cup
Horse shoes
Hollow ware (tea sets, etc.)
Ice cream freezers for home use
Jewelry, all types (except religious goods)
Kick plates
Kitchen utensils and tools, and food processing equipment (except cooking and baking utensils)
Ladders and step stools (except industrial and fire)
Lawn and garden hose accessories, such as sprinklers, nozzles, couplings, clamps, menders, and reels
Lawn mowers, seeders, rollers and tampers
Ledger books
Letter openers
Lightning rods
Luggage fittings, trim and hardware
Machines: rowing, voting
Mail boxes
Maps and globes (world)
Marine construction:
  Boats: pleasure boats and fittings of all kinds
  Canoes
  Rowboats
  Sailboats
Markers:
  grave
  license plates
  price
  tee
  traffic
  tree
Medicine cabinets
Memorials and tablets
Mesh bags
Metal lath
Metal letters and numbers
Mops
Mouldings and trim
Mud scrapers
Nursing bottles
Oil cloth, foil-covered
Ornaments, Christmas tree
Packaging:
  Containers for:
    Bath salt
    Cosmetic, except collapsible tubes
    Gift
    Powder
    Tube, for cigar
  Jars, beauty cream
  Shakers, talcum powder
  Foil for:
    Capsules
    Cartons, liquor
    Florist
    Household
    Labels
    Over wraps (except food)
    Wraps: gift, cosmetic, liquor
    Wine bottle
Paper clips
Plates: name, scuff (except instruction plates on equipment)
Playground equipment
Pleasure boat fastenings, fittings and hardware
Portable bleachers
Push plates
Roofing, residential type (including shingles).
Rulers
Saddlery, and harness hardware
Screening (except insect wire screening)
Shoe heels
Shovels, scoops, scrapers and pushers, (except as required for handling chemical products and grain)
Siding, (except industrial)
Signs, including advertising
Smokers' accessories
Soap dishes
Souvenirs and novelties, advertising specialties
Spandrels
Spools: wire, adhesive tape
Sporting goods, all kinds (except commercial fishery goods)
Spray guns (except paint spraying equipment and agricultural sprays)
Spurs, climbing
Statuary (except religious and artists originals)
Stencils
Store fronts, (except glass holding members)
Stove pipe
Tent poles, frames and pegs
Thermostatic containers, (except shoulders and cups on vacuum bottles of one quart and under size)
Toilet seats and covers
Tokens (except where necessary for electrical operation)
Tombstones
Tooth brush and tumbler holders
Towel bars
Toys
Tricycles and other children's vehicles
Umbrellas and parasols
Venetian blinds, fittings and accessories
Vending machines (except functional parts)
Waste baskets
Wheel barrows (except as required for handling chemicals)
Whistles
Windows, storm (except sash slides)

LIST B

(See section 6)

The use of the forms and products of aluminum defined in section 3 in the items listed below (excluding repair parts) is subject to the prohibitions in this order, except as otherwise stated in this order:

Ducts
Windows, residential type
Windows, non-residential type

SEC. 21. *Base period; applications for adjustment; December 1950 use.* (a) Section 5 (a) of the regulation states, among other things, that no person shall use in manufacture (as defined) or construction "during December 1950 a quantity by weight of aluminum in excess of 100 percent of his average monthly use during the base period."

(b) "Base period" is defined by section 2 (b) as the 6 months' period ending June 30, 1950.

(c) Section 10 states, in part, that "any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue and exceptional hardship upon him not suffered generally by others in the same trade or industry * * *"

(d) A number of requests for adjustment have been filed with the National Production Authority upon the ground that the applicants' business operations were commenced during or after the base period, or that the application of the base period to the applicants' business operations otherwise caused undue hardship upon the applicants not suffered generally by others in the same trade or business. Since many of these applications present common problems, this direction will constitute a determination of adjustment with respect to the limitation stated in section 5 (a) to the classes of cases described below, whether or not applications for adjustment have been filed with the National Production Authority under section 10. This determination is subject, however, to the conditions stated in paragraph (e) of this section.

(e) (1) Cases in which it is claimed that the base period specified in sections 1 to 13, inclusive, is inapplicable because: (i) The applicants commenced new business operations during or after the base period; (ii) although the applicants' business operations were commenced prior to the base period, the applicants produced or manufactured a new product during or after the base period; or (iii) the applicants brought additional productive or manufacturing capacity into operation during or after the base period.

(i) *Direction.* In any such case the applicant may apply as a measure of his permitted use of aluminum during December 1950, his average monthly use during October and November 1950.

(ii) *Illustration 1.* The X Company, a newly organized company, commenced its operations on March 15, 1950. This company will be permitted to use in manufacture or construction during December 1950 a quantity by weight of aluminum not in excess of 100 percent of his average monthly use of aluminum during October and November 1950.

(iii) *Illustration 2.* The Y Company had been engaged in the manufacture of several products incorporating aluminum. Subsequent to June 30, 1950, this company manufactured and marketed an additional line of products, requiring aluminum, not previously manufactured by it. The rule stated in Illustration 1 above applies to the use of aluminum during December 1950 in the manufacture of the new line of products. However, the limitation stated in section 5 (a) applies to the use of aluminum in manufacturing the company's other products.

(iv) *Illustration 3.* During August 1950, the A Company commenced operations for the first time in a new, additional plant. The A Company may use the months of October and November 1950 as the base period for the new plant whereas the base period specified in sections 1 to 13, inclusive, will apply to the operation of its original manufacturing facilities.

(2) Cases in which it is claimed that the base period specified in the order is inapplicable because of changes made during or after the base period in the design, specifications or operating features of certain of its products, and where these changes required the use of substantially larger quantities of aluminum to maintain the same unit output than were required during the base period specified in sections 1 to 13, inclusive.

(i) *Direction.* In any such case, the applicant may apply as a measure of his permitted use of aluminum during December 1950, his average monthly use during October and November 1950.

(ii) *Illustration 1.* During June 1950 the B Company redesigned a machine, its sole product, which it had manufactured and marketed for a number of years and its plant was retooled for its production. In order to conserve weight, aluminum was substituted for steel in various elements resulting in a 30 percent increase in the quantity of aluminum required for the manufacture of the machine. The B Company will be permitted to use in manufacture during December 1950 a quantity by weight of aluminum not in excess of 100 percent of its average monthly use of aluminum during October and November 1950.

(3) Cases in which it is claimed that the applicants' operations were substantially interrupted during the base period.

(i) *Direction.* In any such case in which production or manufacturing operations were shut down or suspended for more than 15 consecutive calendar days, the applicant in determining his base period may exclude from the base period specified in sections 1 to 13, inclusive, the month or months in which shut down or suspension existed.

(ii) *Illustration 1.* The C Company was shut down from February 16 through March 5, 1950. Its base period will comprise the months of January, April, May and June 1950.

(4) Cases in which it is claimed that operations during December 1950 cannot be fairly measured by the base period specified in sections 1 to 13, inclusive, because of seasonal fluctuations which will result in a substantially higher level of operations during December than the average rate of operations during the first six months of 1950.

(i) *Direction.* In any such case, in order to allow for the seasonal factor, the following formula may be applied: The ratio between the total quantity of aluminum used during December of the years 1947, 1948 and 1949, and the total quantity of aluminum used during the first six months of said years. Such ratio may be applied to the total quantity of aluminum used in the first six months of 1950 to determine the quantity that may be used during December 1950.

(ii) *Illustration 1.* By reason of a seasonal demand for its products, the E Company normally schedules its manufacturing operations during December at a rate substantially higher than the average monthly rate that prevailed during the first six months of the year. The ratio between the total quantity of aluminum used in the products manufactured by the E Company during December 1947, 1948 and 1949 and the total quantity of aluminum used during the first six months of these years is 20 percent. Accordingly, the company may use during December 1950 20 percent of the total quantity of aluminum used by it during the first six months of 1950.

(f) The above determinations of adjustment with respect to the classes of cases described are subject to the following conditions: (1) That every person relying on any such determination will promptly after December 1, 1950 prepare a detailed written record of the facts relating to the application of the determination to his operations and preserve same; (2) that a copy of such record will be promptly transmitted to the National Production Authority upon its request; and (3) that such record and all other records relating to production or manufacture and the use of aluminum forms and products listed in section 3 during 1950, and 1947, 1948, and 1949 to the extent applicable, will be made available at his usual place of business for inspection and audit by duly authorized representatives of the National Production Authority. [Direction 1]

SEC. 22. *Base period; applications for adjustment; use during first calendar quarter of 1951.* (a) (1) Section 5 (b) states, among other things, that no person shall use in manufacture (as defined) or construction "during the following months a total quantity by weight of aluminum in excess of the percentages specified with respect to each month of his average monthly use of aluminum during the base period:

| | *Percent* |
|---|---|
| January 1951 | 80 |
| February 1951 | 75 |
| March 1951 | 65" |

(2) "Base period" is defined by section 2 (b) as the 6 months period ending June 30, 1950.

(3) Section 10 states, in part, that "any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue and exceptional hardship upon him not suffered generally by others in the same trade or industry."

(4) A number of requests for adjustment have been filed with the National Production Authority upon the ground that the applicants' business operations were commenced during or after the base period, or that the application of the base period to the applicants' business operations otherwise caused undue hard-

ship upon the applicants not suffered generally by others in the same trade or business. Since many of these applications present common problems, this direction will constitute a determination of adjustment with respect to the limitation stated in section 5 (b) to the classes of cases described below, whether or not applications for adjustment have been filed with the National Production Authority under section 10. This determination is subject, however, to the conditions hereinafter stated.

(i) Cases in which it is claimed that the base period specified in the order is inapplicable because: (1) The applicants commenced new business operations during or after the base period; or (2) although the applicants' business operations were commenced prior to the base period, the applicants produced or manufactured a new product during or after the base period.

(*a*) *Direction.* In any such case the applicant may apply as a measure of his permitted use of aluminum during the first quarter of 1951 as specified in the percentage limitations stated in section 5 (b), his average monthly use during October and November 1950.

(*b*) *Illustration 1.* The X Company, a newly organized company, commenced its operations on March 15, 1950. This company will be permitted to use in manufacture or construction during the following months a total quantity by weight of aluminum not in excess of the percentages specified with respect to each month of his average monthly use of aluminum during October and November 1950:

| | *Percent* |
|---|---|
| January 1951 | 80 |
| February 1951 | 75 |
| March 1951 | 65 |

(*c*) *Illustration 2.* The Y Company had been engaged in the manufacture of several products incorporating aluminum. Subsequent to June 30, 1950, this company manufactured and marketed an additional line of products, requiring aluminum, not previously manufactured by it. The rule stated in Illustration 1 above applies to the use of aluminum during the first quarter of 1951 in the manufacture of the new line of products. However, the limitation stated in section 5 (b) as amended, applies to the use of aluminum in manufacturing the company's other products.

(ii) Cases in which it is claimed that the base period specified in the order is inapplicable because of changes made during or after the base period in the design, specifications or operating features of certain of its products, and where these changes required the use of substantially larger quantities of aluminum to maintain the same unit output than were required during the base period specified in the order.

(*a*) *Direction.* In any such case, the applicant may apply as a measure of his permitted use of aluminum during the following months a quantity by weight of aluminum not in excess of the following percentages specified with respect to each month of the quantity of aluminum that he would have used on an average monthly basis during the base period if during said period his products had been manufactured in accordance with the changed design, specifications or operating features:

| | *Percent* |
|---|---|
| January 1951 | 80 |
| February 1951 | 75 |
| March 1951 | 65 |

(*b*) *Illustration 1.* During July 1950 the A Company redesigned a machine, its sole product, which it had manufactured and marketed for a number of years and its plant was retooled for its production. In order to conserve weight, aluminum was substituted for steel in various elements of the machine. In manufacturing this machine during the base period and prior to its redesign, 2 lbs. of aluminum had been required for each machine whereas each machine as redesigned required 3 lbs. of aluminum. The average monthly use of aluminum by A Company for this purpose during the base period was 1,000 lbs. During January 1951, the A Company will be permitted to use in manufacture a quantity by weight of aluminum not in excess of 80 percent of 1,500 lbs. of aluminum.

(iii) Cases in which it is claimed that the applicants' operations were substantially interrupted during the base period.

(*a*) *Direction.* In any such case in which production or manufacturing operations were shut down or suspended for more than 15 consecutive calendar days, the applicant in determining his base period may exclude from the base period specified in the order the month or months in which the shutdown or suspension existed.

(*b*) *Illustration 1.* The B Company was shut down from February 16 through March 5, 1950. Its base period will comprise the months of January, April, May, and June 1950.

(b) (1) The above determinations of adjustment with respect to the classes of cases described are subject to the following conditions: (i) That every person relying on any such determination will promptly after January 1, 1951, prepare a detailed written record of the facts relating to the application of the determination to his operations which will be signed by such person or by an authorized officer or representative, and preserve same, such record to include (*a*) use permitted under the order as amended, of the aluminum forms and products listed in section 3 during the first quarter of 1951, (*b*) permitted use of such forms and products during said quarter under this section and (*c*) basis of computation; and (ii) that such record shall be retained for at least two years and will be made available at his usual place of business for inspection and audit by duly authorized representatives of the National Production Authority.

(2) The National Production Authority reserves the right to modify or revoke adjustments made pursuant to this section. Any person affected by such a modification or revocation will be notified in writing of the nature of the action taken and the reasons therefor. Such actions will be effective upon such date or dates subsequent to the date of the notification as are specified therein.

[Direction 2]

SEC. 23. *Application for adjustment—component parts.* (a) (1) Section 5 (b) states, among other things, that no person shall use in manufacture (as defined) or construction during March 1951 a total quantity by weight of aluminum in excess of 65 percent of his average monthly use of aluminum during the base period. The base period is defined by section 2 (b) as the six months period ending on June 30, 1950.

(2) Section 10 states, in part, that "any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue and exceptional hardship upon him not suffered generally by others in the same trade or industry."

(3) A number of requests for adjustment have been filed with the National Production Authority on the ground that the permitted use of aluminum in March 1951 for the manufacture of certain component parts requiring relatively small amounts of aluminum will unduly curtail the production of the end products for which these components are designed and would not be in the public interest. The following direction will constitute a determination of adjustment with respect to the limitation stated in section 5 (b) to the manufacture of component parts hereinafter described whether or not applications for adjustment have been filed with the National Production Authority.

(b) Direction: Any person who manufactures any component parts made wholly or partly of aluminum may use a total quantity by weight of aluminum in the manufacture of such component parts during March 1951 not in excess of 75 percent of his average monthly use of aluminum for this purpose during the base period: *Provided,* That (1) such component parts serve a functional purpose in the end product; (2) it is not practicable to substitute another material for aluminum before or during March 1951; (3) the total weight of the aluminum in such component parts in the end product is less than 1 percent of the total weight of the end product; and (4) the manufacturer of such component parts obtains a signed certification from the manufacturer or assembler of the end product evidencing the facts set forth in subparagraphs (1), (2) and (3) of this paragraph.

(c) (1) The above determination of adjustment is subject to the following conditions: (i) That every person relying on such determination shall on or before April 1, 1951, prepare a detailed written record of the facts relating to the application of the determination to his operations which will be signed by such person or by an authorized officer or representative; and (ii) that such record will be retained for at least two years and will be made available at his usual place of business for inspection and audit by duly authorized representatives of the National Production Authority.

(2) The National Production Authority reserves the right to modify or revoke adjustments made pursuant to this section. Any person affected by such a

modification or revocation will be notified in writing of the nature of the action taken and the reasons therefor. Such action will be effective upon such date or dates subsequent to the date of notification as are specified therein. [Direction 3]

[F. R. Doc. 51-3283; Filed, Mar. 9, 1951; 5:06 p. m.]

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[NPA Order M-12 as Amended Mar. 9, 1951]

## M-12—Use of Copper and Copper-Base Alloys

This amendment to NPA Order M-12 is found necessary and appropriate to promote the national defense and is issued pursuant to the Defense Production Act of 1950. In the formulation of this order, there has been consultation with industry representatives, including trade association representatives, and consideration has been given to their recommendations. However, consultation with representatives of all trades and industries affected in advance of the issuance of this order has been rendered impracticable due to the necessity for immediate action and because the order affects a large number of different trades and industries.

This amendment affects NPA Order M-12, as previously amended, as follows: It amends paragraphs (a) and (b) of section 5, paragraphs (c) and (d) of section 6, revises section 9, adds paragraph (c) to section 11, and amends Lists A and B. As so amended, NPA Order M-12 reads as follows:

Sec.



Authority: Sections 1 to 15 issued under sec. 704, Pub. Law 774, 81st Cong. Interpret or apply sec. 101, Pub. Law 774, 81st Cong.; sec. 101, E. O. 10161, Sept. 9, 1950, F. R. 6105 3 CFR, 1950 Supp., sec. 2, E. O. 10200, Jan. 3, 1951, 16 F. R. 61,

Section 1. *What this order does.* The purpose of this order is to describe how the copper remaining after allowing for the requirements of national defense may be distributed and used in the civilian economy. It is the policy of the National Production Authority that copper and articles made of copper, not required to fill rated orders, shall be distributed equitably through normal channels of distribution, and that due regard shall be given by suppliers to the needs of new and small business. It is the intent of this order that other materials which are not in short supply shall be substituted for copper and copper-base alloy wherever possible.

Sec. 2. *Definitions.* As used in this order:

(a) "Person" means any individual, corporation, partnership, association or any other organized group of persons and includes any agency of the United States or any other government.

(b) "Base period" means the six-months period ending June 30, 1950.

(c) "Manufacture" means to put into process, machine, incorporate into products, fabricate or otherwise alter the forms and products of copper defined in section 3 by physical or chemical means, and includes the use of copper in plating.

(d) "Maintenance" means the minimum upkeep necessary to continue a building, machine, piece of equipment or facility in sound working condition, and "repair" means the restoration of a building, machine, piece of equipment or facility to sound working condition when the same has been rendered unsafe or unfit for service by wear and tear, damage, failure of parts or the like: *Provided, however,* Neither maintenance nor repair includes the improvement of any such item with materials of a better kind, quality or design.

(e) "Operating supplies" means any copper or copper-base alloy forms or products listed in section 3 which are normally carried by a person as operating supplies according to established accounting practice and are not included in his finished product, except that materials included in such product which are normally chargeable to operating expense may be treated as operating supplies.

Sec. 3. *Copper forms and products to which this order applies.* This order applies to the following forms and products of copper: Copper, copper-base alloy, brass mill products, copper wire mill products, and foundry copper products and copper-base alloy products. For the purpose of this order, these items are defined as follows:

(a) "Copper" means unalloyed copper. (It includes electrolytic copper, fire refined copper and all unalloyed copper in any form including scrap.)

(b) "Copper-base alloy" means any alloy in the composition of which the percentage of copper metal by weight equals or exceeds 40 percent of the total weight of the alloy. (It shall include fired and demilitarized cartridge and artillery cases, and all copper-base alloy, as specified above, in any form including scrap.) It does not include alloyed gold produced in accordance with U. S. Commercial standard CS67-38.

(c) "Brass mill product" means sheet, including strip and plate; rod, including bars, forgings (rough as forged), and extruded shapes; wire; or tube, including pipe; made from copper or copper-base alloy. This does not include copper wire mill products.

(d) "Copper wire mill product" means bare wire, insulated wire and cable whatever the outer protective coverings may be, and uninsulated wire and cables, where the conductors are made from copper, copper-base alloy, or copper clad steel containing over 20 percent copper by weight. All copper wire mill products should be measured in terms of pounds of copper content.

(e) "Foundry products" means cast copper and copper-base alloy shapes or forms suitable for ultimate use without remelting, rolling, drawing, extruding or forging. (Includes the removal of gates, risers and sprues, and sandblasting, tumbling, or dipping, but excludes any further machining or processing.)

Sec. 4. *Application of order.* Subject to the exemptions stated in section 9, this order applies to all persons who produce brass mill products, copper wire mill products or foundry products as listed in section 3, or who use any of the forms and products of copper defined in paragraphs (a), (b), (c), (d) and (e) of section 3 for the purpose of manufacture, use in installation or construction, or for maintenance, repair or operating supplies. This order also contains limitations on the use of such copper forms and products in the manufacture or assembly of certain items. This order does not apply to persons who use copper or copper-base alloy in the production of other metals or metal alloys.

Sec. 5. *Production of brass mill products, copper wire mill products and foundry products.* Subject to the exemptions stated in section 9 or unless specifically directed by the National Production Authority:

(a) No person shall produce during the following months a total quantity by weight of brass mill products and copper wire mill products in excess of the percentages specified with respect to each month of his average monthly production of such products during the base period:

| | Percent |
|---|---|
| January, 1951 | 85 |
| February, 1951 | 85 |
| March, 1951 | 80 |

During the calendar quarter commencing on April 1, 1951, no person shall produce a total quantity by weight of brass mill products and copper wire mill products in excess of 80 percent of his average quarterly production of such products during the base period: *Provided, however,* That such production in any one month shall not exceed 40 percent of the permitted quarterly production. The production of brass mill products and copper wire mill products, pursuant to a valid toll or conversion agreement or other arrangement whereby title to the material to be processed remains vested in the person who delivers it, is permitted in addition to the production permitted by this paragraph. In determining average monthly production during the base period, the brass mill products and copper wire mill products so produced shall not be included in the base period production of the brass mill or wire mill. Nothing contained in this paragraph shall affect the restrictions on toll and other similar agreements contained in NPA Order M-16.

(b) During each of the calendar quarters commencing on January 1, 1951, and April 1, 1951, no person shall produce a total quantity by weight of foundry products in excess of 100 per-

cent of his average quarterly production of foundry products during the base period.

SEC. 6. *Use of copper forms and products.* Subject to the exemptions stated in section 9, or unless specifically directed by the National Production Authority, no person shall use in manufacture, installation or construction:

(a) During December 1950, a total quantity by weight of the forms and products of copper defined in paragraphs (a), (b), (c), (d) and (e) of section 3 in excess of 100 percent of his average monthly use of such material in October and November 1950.

(b) During the following months a total quantity by weight of the forms and products of copper defined in paragraphs (a), (b), (c), and (d) of section 3 (including copper forms and products produced under toll and conversion agreements or other similar arrangements) in excess of the percentages specified with respect to each month of his average monthly use of such material during the base period:

| | Percent |
|---|---|
| January, 1951 | 85 |
| February, 1951 | 85 |
| March, 1951 | 80 |

(c) During the calendar quarter commencing on April 1, 1951, a total quantity by weight of the forms and products of copper defined in paragraphs (a), (b), (c), and (d) of section 3 (including copper forms and products produced under toll and conversion agreements or other similar arrangements) in excess of 75 percent of his average quarterly use of such copper during the base period: *Provided, however,* That such use in any one month shall not exceed 40 percent of the permitted use.

(d) During each of the calendar quarters commencing on January 1, 1951, and April 1, 1951, a total quantity by weight of foundry products in excess of 100 percent of his average quarterly use of such products during the base period: *Provided, however,* That in cases where a foundry product in the form of a casting is owned by one person and machined pursuant to a contractual agreement by another person, it shall be considered that the owner used the casting in manufacture.

SEC. 7. *Prohibited uses of copper.* (a) Commencing on March 1, 1951, no person shall use copper in the forms and products defined in section 3, or any component part made therefrom, in the manufacture or assembly of any item included in attached List A, except as permitted therein; and no person shall use in the manufacture or assembly of any item, whether or not included in List A, a greater quantity or better grade of such materials than is necessary for functional or operational purposes, or use such materials solely for decorative or ornamental purposes. However, these prohibitions shall not apply to such use of: (1) Any such copper forms and products, or component parts made therefrom, on or after March 1, 1951, if such materials were contained in such person's inventory on said date and are wholly unsuitable for use in the manufacture or assembly by such person of any item not included in List A; or (2) any such materials covered by an order placed with a producer and included in the producer's schedule for February 1951, which are delivered to such person at his plant prior to April 1, 1951, to the extent that such materials are wholly unsuitable for use in manufacture or assembly by such person of any item not included in List A. Every person who relies on the provisions of the next preceding sentence shall prepare a detailed record showing: (A) The quantities of such copper forms and products, and component parts made therefrom, which were contained in his inventory on the first days of December 1950, and of January, February and March 1951, and which were wholly unsuitable for use in his manufacture or assembly of any item not included in List A; and (B) the quantities of such materials wholly unsuitable for such use which were delivered to him on or after March 1, 1951, the names and addresses of the suppliers thereof, and the dates of the orders and acceptances covering such materials together with the applicable mill schedule. Such record shall be retained for at least two years and shall be made available at the usual place of business where maintained for inspection and audit by duly authorized representatives of the National Production Authority.

(b) Commencing on April 1, 1951, no person shall use copper in the forms and products defined in section 3, or any component part made therefrom, in the manufacture or assembly of any item included in attached List B, except as permitted therein. However, this prohibition shall not apply to such use of: (1) Any such copper forms and products, or component parts made therefrom, on or after April 1, 1951, if such materials were contained in such person's inventory on said date and are wholly unsuitable for use in the manufacture or assembly by such person of any item not included in List A or List B; or (2) any such materials that have been covered by any order placed with a producer which were included in the producer's schedule for March 1951, and are delivered to such person at his plant prior to May 1, 1951, to the extent that such materials are wholly unsuitable for use in manufacture or assembly by such person of any item not included in List A or List B. Every person who relies on the provisions of the next preceding sentence shall prepare a detailed record showing: (A) The quantities of such copper forms and products, and component parts made therefrom, which were contained in his inventory on the first days of January, February, March and April 1951, and which were wholly unsuitable for use in his manufacture or assembly of any item not included in List B; and (B) the quantities of such materials wholly unsuitable for such use which were delivered to him on or after April 1, 1951, the names and addresses of the suppliers thereof, and the dates of the orders and acceptances covering such materials, together with the applicable mill schedule. Such record shall be retained for at least two years and shall be made available at the usual place of business where maintained for inspection and audit by duly authorized representatives of the National Production Authority.

(c) Notwithstanding the provisions of paragraphs (a) and (b) of this section, copper or copper-base alloy may be used: (1) For plating any item included in List A or List B, or any component part thereof, where such plating is an undercoat for chromium, nickel, gold or silver; or (2) for brazing any item, or component part thereof, included in List A or List B.

(d) During February 1951, no person shall use in the manufacture or assembly of the items included in attached List A a total quantity by weight of the copper forms or products defined in paragraphs (a), (b), (c) and (d) of section 3, or any component part made therefrom, in excess of 85 percent, or of the foundry products defined in paragraph (e) of said section, or any component part made therefrom, in excess of 100 percent, of his average monthly use of such materials for such purposes during the base period. During March 1951, the same limitations shall apply to the manufacture or assembly of the items included in attached List B, except that the percentage limitation as to the copper forms and products defined in paragraphs (a), (b), (c) and (d) of section 3 shall be 80 percent instead of 85 percent. To the extent that manufacture or assembly of the items on attached List A or List B is permitted under paragraphs (a) or (b) of this section, the limitations of section 6 shall also apply during March 1951 and each succeeding month.

(e) Commencing on April 1, 1951, no person shall use in construction any brass mill product as such for any item included in List A or List B except as permitted therein.

(f) The following items included in List A or List B shall be exempt from the application of this section if they are used on vessels other than pleasure craft: (1) Furnishings, fittings, and fixtures when located within the sphere of the magnetic compasses; and (2) builders' hardware, building materials and snap hooks where the properties supplied by copper are essential and satisfactory substitutes not available.

(g) The prohibitions of this section apply notwithstanding the provisions of NPA Reg. 2 with respect to the filling of rated orders and are not affected by any of the exemptions stated in section 9: *Provided, however,* That such provisions of NPA Reg. 2 and paragraphs (a) and (b) of section 9 apply to such items included in attached List A or List B as are specifically designated as being permitted for the use of the Armed Forces of the United States, including the United States Coast Guard.

SEC. 8. *Maintenance, repair and operating supplies.* Unless specifically directed by the National Production Authority, during the calendar quarter commencing on January 1, 1951, and each calendar quarter thereafter, no person shall use for maintenance, repair and operating supplies a quantity by weight of the forms and products of copper defined in paragraphs (a), (b),

(c), (d) and (e) of section 3 in excess of 100 percent of his average quarterly use for such purposes during the base period.

SEC. 9. *Exemptions.* (a) The production of brass mill, copper wire mill and foundry products and the use of such products is permitted to fill rated orders, or to meet any mandatory order of the National Production Authority, in addition to the production and use permitted by the provisions of sections 5, 6 and 8.

(b) Copper forms and products defined in section 3 acquired with ratings, or to meet a National Production Authority scheduled program may be used in addition to the quantities permitted by the provisions of sections 6 and 8.

(c) The provisions of sections 6 and 8 do not apply to persons who use less than 1,000 lbs. of the copper forms and products defined in section 3 during any calendar quarter; *Provided, however,* That persons who by reason of the provisions of sections 6 and 8 would be permitted to use less than 1,000 lbs. during any calendar quarter, may use during such period a quantity up to 1,000 lbs.

SEC. 10. *Inventories.* In addition to the provisions of NPA Reg. 1 relating to Inventory Controls, it is considered that a more exact requirement applying to producers of brass mill products, copper wire mill products and foundry products, and to users of the copper forms and products defined in section 3 is necessary.

(a) No person producing brass mill products, copper wire mill products or foundry products may receive or accept delivery of copper or copper-base alloy if his inventory is, or by such receipt would become, in excess of that necessary to meet his deliveries or supply his services on the basis of his scheduled method and rate of operation pursuant to this order during the succeeding 45-day period, or in excess of a "practicable minimum working inventory" (as defined in NPA Reg 1, whichever is less.

(b) No person obtaining copper forms or products defined in section 3 for use in manufacture, installation or construction, or for maintenance, repair or operating supplies, may receive or accept delivery of a quantity of such forms and products if his inventory is, or by such receipt would become, in excess of that necessary to meet his deliveries or supply his services on the basis of his scheduled method and rate of operation pursuant to this order during the succeeding 60-day period, or in excess of a "practicable minimum working inventory" (as defined in NPA Reg. 1), whichever is less.

(c) For the purpose of this section, any copper forms and products defined in section 3, in which minor changes or alterations have been effected, shall be included in inventory. NPA Reg. 1 will apply to all such forms and products except as modified by this section.

SEC. 11. *Restrictions on delivery.* (a) No person shall deliver any of the forms and products of copper defined in section 3 if he knows or has reason to believe that his customer may not accept delivery of such materials under this order or will use such materials in violation of this order.

(b) No person shall deliver any copper forms or products defined in section 3 unless the purchaser shall have furnished to the seller a signed certification as follows:

> The undersigned, subject to statutory penalties, certifies that acceptance of delivery and use by the undersigned of the copper forms or products herein ordered will not be in violation of NPA Order M-12.

This certification constitutes a representation by the purchaser to the seller and to the National Production Authority that delivery of such copper forms or products may be accepted by the purchaser under this order, and that such materials will not be used by the purchaser in violation of this order.

(c) The certification required by paragraph (b) of this section shall not be required in connection with the delivery of copper forms and products (1) to the General Services Administration for the stockpile of strategic materials, (2) to purchasers where delivery is made prior to April 1, 1951, pursuant to an order received prior to February 19, 1951, (3) to purchasers of quantities weighing 25 pounds or less, or (4) to purchasers in foreign countries.

SEC. 12. *Applications for adjustment.* Any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue or exceptional hardship upon him not suffered generally by others in the same trade or industry, or its enforcement against him would not be in the interest of the national defense or in the public interest. In considering requests for adjustment claiming that the public interest is prejudiced by the application of any provision of this order, consideration will be given to the requirements of the public health and safety, civilian defense, and dislocation of labor and resulting unemployment that would impair the defense program. Producers shall make such application on Form NPAF-11, "Copper and Copper-Base Alloys: Producer's application for Adjustment or Exception." Users shall make application on Form NPAF-12, "Copper Forms and Products: User's Application for Adjustment or Exception." Copies of these forms may be obtained from the nearest Department of Commerce Field Office.

SEC. 13. *Records and reports.* (a) Persons subject to this order shall preserve the records which they have maintained of production, inventories, receipts, deliveries and uses of copper forms and products defined in section 3 commencing with January 1, 1950.

(b) Persons subject to this order shall make records and submit such reports to the National Production Authority as it shall require subject to the terms of the Federal Reports Act (Pub. Law 831, 77th Cong., 5 U. S. C. 139-139F).

SEC. 14. *Communications.* All communications concerning this order shall be addressed to the National Production Authority, Washington 25, D. C. Ref: M-12.

SEC. 15. *Violations.* Any person who wilfully violates any provisions of this order or any other order or regulation of the National Production Authority or wilfully conceals a material fact or furnishes false information in the course of operation under this order is guilty of a crime and upon conviction may be punished by fine or imprisonment or both. In addition, administrative action may be taken against any such person to suspend his privilege of making or receiving further deliveries of materials or using facilities under priority or allocation control and to deprive him of further priorities assistance.

This order, as amended, (includes Lists A and B hereto attached. The order as amended including Lists A and B shall take effect, except as otherwise specifically stated, on March 9, 1951.

NATIONAL PRODUCTION AUTHORITY,
[SEAL] MANLY FLEISCHMANN,
*Administrator.*

LIST A

(See section 7)

The use of the forms and products of copper defined in section 3 and of any component parts made therefrom in the items listed below (excluding repair parts) is prohibited except to the extent permitted in the order or the list: *Provided, however,* That such material may be used in such items included in the list as are marked with an asterisk in cases where such items are to be used by the Armed Forces of the United States, including the United States Coast Guard.

BUILDERS' HARDWARE

Protective brass plating of all listed items of builders' hardware is permitted where other types of finishes are not practicable.
Butts, hinges and related items.
Checking floor closers, overhead concealed, semi-concealed and surface door closers (except gland nuts, regulating screw assemblies, and fusible links).
Closers, hanging brackets for.
Closers, screen door.
Cabinet hardware, including cabinet hinges.
Hangers, track and related items including:
  Sliding door hardware.
  Folding door hardware.
  Sliding-folding door hardware.
  Folding partition hardware.
  Upward acting door hardware.
  Fire door hardware (except bearings and fusible links).
Hardware for sash, screen, transom and casement and other shelf hardware items.
Locks, lock trim (except for cylinder assemblies and keys, for essential working parts of locks and latches, for faces of locks and latches and for trim of cylinder lock sets).
Spring hinges.
Sash balances.
Door holding devices.
Kick plates.
Push plates.
Door pulls.
Push bars.
House numbers.
Door knockers.
Letter boxes.
Nameplates.

BUILDING MATERIALS

Anchors and dowels (except window cleaner's safety anchors).
Bands on pipe insulation.

Bathtub enclosures and shower enclosures.
Blinds, including fixtures and fittings (except where essential for operating parts).
Caulking anchors.
Cement flooring and composition flooring (except that crude arsenical copper precipitate may be used for flooring in hospital operating and anesthesia rooms, for places where explosives are handled or stored and for places where explosive vapors may be present).
Chimneys and flues.
Conduits (except instrument assemblies).
Cornices.
Door sills.
Door frames.
Doors.
Downspouts and accessories thereto.
Drains (except strainer grids for showers and urinals).
Drip pans.
Elevators and escalators (except for worm gears and parts for conducting electricity).
Escutcheons and plates for floor, ceiling and wall use.
Fences and gates.
Food waste disposal units (except current-carrying parts, bearings, controls, impellers and sink strainers).
Gratings.
Grids (except for flooring in hospital operating rooms and anesthesia rooms, and for places where explosives are handled or stored and for places where explosive vapors may be present).
Grilles and shields, including fresh air inlet boxes and radiator and convector enclosures.
Gutters and accessories thereto.
Holdback hooks for curtains.
I. P. S. waste nipples.
Lavatory legs (except for hospital use).
Leaders and accessories thereto.
Linoleum stripping.
Louvres.
Marquees.
Metal siding.
Mouldings for joining cabinet sinks.
Ornamental metal work; including grille work, railings, and fittings.
Pipe, iron pipe sizes and fittings (except for industrial process piping and chemical and gas equipment and except for solder nipples, solder bushing and ferrules).
Radiator covers and shields.
Railings and fittings.
Reglets, moulding and trim.
Rim protectors for fixtures.
Robe hooks.
Roofing.
Roofing nails (except staples, clips and similar devices designed for the purpose of protecting shingles, flashings and siding against wind damage).
Shower curtain rods and bars (except for hospitals).
Shower door frames.
Shower goosenecks.
Skylights.
Stair and threshold treads, nosing and edgings.
Store fronts.
Straps and hangers for pipe supports.
Supply pipes, iron pipe sizes.
Switch plates.
Tanks for automatic storage water heaters.
Traps (except tube traps in 20 gauge without cleanouts and except traps cast from secondary metal).
Thresholds and saddles.
Towel bars and brackets.
Tube, tubing and fittings for piping systems in construction (except for Type K for underground water service connections; Types B, L, and M for domestic hot and cold water supply pipes, tank to oil burner hook-ups, and oxygen lines; Types B, K, L, and M for industrial process, food, chemical and gas equipment piping; and seamless tube for air temperature control apparatus).
Unit heaters, unit ventilators, unit ventilator inlet wall boxes and convectors, and blast heating coils, or any apparatus using such coils as part of its construction (except for valves, controls, fins, bearings or parts necessary for conducting electricity, and for water or steam courses and headers).
Ventilators.
Vents.
Weatherstripping.
Window frames.
Window sills.
Windows.

BURIAL EQUIPMENT

Burial urns.
Burial vaults.
Caskets and casket hardware (except copper or brass flash plate treatment necessary to prevent corrosion during period of manufacture and warehousing).
Memorial tablets.

CLOTHING AND DRESS ACCESSORIES, NOT INCLUDING SAFETY EQUIPMENT

Artificial flowers.
*Buckles and shoe buckles (except for foundation garments where strength, launderability and non-corrosiveness are essential).
*Buttons (except front shells of uniform buttons for police, firemen, guards, railroad and other transportation employees and similar uniforms, the backs to be made of steel with rust resistant plating; and work clothing and other utility (closure) purposes where launderability and non-corrosiveness are essential, provided that all strictly decorative and out-size buttons are eliminated).
Dress ornaments and trimmings.
*Fittings: belt, corset, garter, glove, hand bag, purse, suspender, luggage and supporter (except for foundation garments and sanitary belts where launderability and non-corrosiveness are essential).
*Insignia and decorations (awards).
*Metal clothes, laces, tassels, braids, embroidery, ribbons.
Millinery accessories and frames.
*Snaps, snap buttons, and hooks and eyes (except (1) irrespective of weight, in industrial safety clothing, work clothing and foundation garments; (2) for complete fasteners weighing 5 pounds or less per thousand units, on other wearing apparel exclusive of belts, suspenders, gloves, footwear, and other dress accessories, and billfolds, luggage, wallets and key cases; and (3) except for wire springs contained in snaps and snap buttons weighing in excess of 5 pounds per thousand complete units).

FURNISHINGS AND EQUIPMENT

Andirons, fireplace screens and fittings.
Candlesticks.
Curtain fasteners, rods and rings.
Cuspidors.
Gas heater and stove installation connections (except for high pressure LPG connections from tank to fixture).
Lamp shades.
Mops.
Mud scrapers.
Scrubbing boards.
Space heaters, flue connected and non-flue connected (except valves, controls and parts necessary for proper operation or for conducting electricity).
Stoves and ranges of all fuels for household cooking use (except valves, compression fittings, controls including timers, thermostats and parts for conducting electricity or necessary for safe operation).
Trays.
Upholsterers' supplies, including nails and tacks.
Vases, pitchers, bowls, and artcraft (except scientific laboratory).
Washing tubs and washing boilers.
Waste baskets, humidors and similar items.

FURNITURE AND FIXTURES

Barber shop and beauty parlor furniture.
Household furniture.
Mattresses and bedsprings (except hospital).
Partitions and shelving (except hospital and laboratory).
Public building and office furniture.
Reed and rattan furniture.
Restaurant furniture.
Venetian blinds (except where essential for operating parts).

HARDWARE, MISCELLANEOUS

Collars and other harness for pets.
Cutlery, table, kitchen, butcher and meat packing (except rivets and knife assemblies in matching silver-plated flatwear sets).
Fireplace fixtures and equipment.
Furniture (except in cylinder assemblies and keys and for essential working parts of locks).
Hand saw screws, nuts and washers for attaching saw blades to the handles.
Hand service tools, including hammers, pliers, wrenches, screw drivers, etc. (except essential parts of spiral ratchet and ratchet screw drivers and drills; hand and breast drills and bit braces; soldering irons; and blow-torches; except nonsparking tools necessary to prevent explosion hazards; and except portable spot welders).
Passenger transportation equipment, decorative hardware and ornamental metal work and trim and general hardware (except for locks).
Pleasure boat decorative hardware.
Pocket knives (except rivets and lining assemblies).
Puttying and scraping knives (except rivets).
*Saddlery and harness hardware (except for brass protective plating).
Scissors, shears, hedge and other trimmers, tinners and other snips.
Stairs and threshold treads and edgings.
Trunk and luggage hardware (except for brass protective plating and except in cylinder assemblies and keys and for essential working parts of locks).

HOUSEHOLD ELECTRICAL APPLIANCES

(Except for operational parts where the properties supplied by the copper are essential or where necessary for electrical conductivity)

Household electrical appliances including but not limited to:

Laundry equipment.
Vacuum cleaners.
Refrigerators.
Floor and furniture polishers.
Food mixers.
Electric irons.
Hair driers.
Toasters.

JEWELRY, GIFTS, AND NOVELTIES

All jewelry (except operational attachments such as screw and snap posts; cam assemblies; wire pegs; screws and/or rivets; spring pins for wrist watches; catches and pin stems; and copper seal interlinings to prevent "bleeding" of silver through gold); gifts and novelties, including but not limited to:

Book ends.
Jewelry and instrument cases, including cosmetic.
Lighters (except necessary operational parts).
*Medals and emblems, including decorations (except religious goods).
Mirror and picture frames.
Napkin rings.
Smokers' accessories, including ash trays and humidors.
Souvenirs.

CIVILIAN TYPE MOTOR VEHICLE: PASSENGER AUTOMOBILES INCLUDING TAXICABS, STATION WAGONS, AMBULANCES, HEARSES, TRUCKS, TRUCK TRACTORS, TRUCK TRAILERS, MOTORCYCLES AND BUSSES

Decorative mouldings, both internal and external (except for glass run channels, window-glass frames, external windshield and rear window external mouldings where such mouldings are produced from strip 6 inches or narrower).
Defrosters and heaters (except (1) for conducting electricity and (2) radiators (heat exchangers) and supply and return hot water lines and (3) parts used in the operating controls of the heating and defrosting systems).
Gas tank caps (except valves and springs).
Horns (except parts for diaphragms, vibrators and conducting electricity).
Lighters (except parts for conducting electricity).
Lights, lamps, headlamps, and lighting accessories (except for doors, bezels, adjusting and attaching screws, retaining rings, copper flash plating on reflectors and parts for conducting electricity including light bulbs).
Motor vehicle hardware (except door handles, ventilator and regulator handles for windows and doors, working parts for locks, ventilator window latches, external lock cylinder caps and covers, external windshield wiper arm and blade assemblies and screw).
Rear-view mirrors and brackets (except copper flash plating on mirrors).
Smokers' accessories, including ash trays.
Wheel discs and wheel trim rings.

PASSENGER TRANSPORTATION EQUIPMENT

(Including railroad cars, street and interurban cars, busses, and trailers, but excluding locomotives)

All items under the heading "Furnishings and Equipment".
Bands on pipe coverings.
Door knockers, checks, pulls and stops.
Doors and windows, door and window frames and window sills.
Drinking water reservoirs.
Shower rods and pans.
Sinks and drainboards.
Towel and luggage racks.
Water containers for humidification.
Weatherstripping and insulation.

MISCELLANEOUS

Alarm and protective systems (except parts for conducting electricity or where essential to the proper service or functioning of the parts).
Antique reproductions.
Arch supports.
Atomizers (except for medicinal purposes and for use in the preparation of dried milk and dried eggs).
Barrels, boxes, cans, jars, and other containers.
*Badges (except for use by personnel where badges are required for protection and security by Government agencies or by industrial plants).
Bar and counter equipment and fittings.
Barber shop equipment and supplies (except for current-carrying parts).
Barrel hooks.
Bathroom accessories (including grab bars, tumbler holders, tooth brush holders, paper holders, and shelf brackets).
Beauty parlor equipment and supplies (except for replacement parts of commercial permanent wave equipment and commercial hair driers and for current-carrying parts).
Bicycles, and similar vehicles and equipment therefor (except valves for bicycle tires and tubes and except plating of operational parts).
Binoculars (except precision types) and opera glasses.
Bird and pet cages and stands.
Branding, marking, and labeling devices and stock for same (except engraved burning branding dies, and except where the devices and the stock are for affixing governmental, notarial and corporate seals).
Bronze ink (except use in the graphic arts industry where bronze ink and powder are an integral part of product identification and whose normal replating is less frequent than one year).
Brushes (except for the types used in electric motors and generators; and except for industrial brushes and tooth brushes).
Carpet rods.
Chimes and bells (except parts for conducting electricity or where non-magnetic gong material is required for electrically operated signaling devices used as adjuncts to communication systems and except bells for use on board ship where essential to the proper functioning of the parts).
Clips, paper.
Cleaning and polishing accessories, such as brooms, carpet sweepers, crumbing sets, dust pans, mops, pot scourers, whisk brooms and floor and furniture polishers.
Clock cases (except for marine use).
Clothes line pulleys and reels.
Cocktail shakers.
Coin-operated game and gambling machines (except tumblers for locks and current-carrying parts).
Coin-operated vending machines (except necessary operational parts and current-carrying parts).
Cooking utensils (except gauges and protective devices and plating of bottoms).
Daubers for shoe polish.
Dispensers, hand, for hand lotions, paper products, soap and straws (except for hospitals).
Flower pots, boxes and holders for same.
Fountain pens (except necessary operational parts).
Furniture grommets.
Garden tools and equipment (except for functional parts).
Hair curlers, hair brushes and combs (except for heat-carrying parts and for electrical conductivity).
Ice cream freezers for use in the home (except electric).
Juke boxes (except for current-carrying parts).
Kitchen utensils, devices and machines (except electrical appliances).
Lace tips.
Lamps, portable electric (except for current-carrying parts).
Lamps and lanterns, other than electric (except for generators, valves, controls, burners, wicks and founts).
Letter boxes and mail chutes.
Lighting fixtures (except (1) current-carrying parts, plating, rivets, eyelets, screws, small fasteners; (2) the threaded parts, clamping, sealing or attachment devices of exterior, explosion-proof, dust-tight and vapor-tight fixtures; (3) Marine and airport).
Loose-leaf binders.
Manicure implements.
Match and pattern plates, matrices, and flasks.
Mattress buttons and furniture glides.
Name plates (except instruction and data plates and identification plates for use on machinery or equipment without display or ornamentation).
Nonoperating or decorative uses of copper or copper-base alloy, or the use of the same in such parts of installations and equipment (mechanical or otherwise) as bases, frames, guards, standards and supports.
Package handles and holders.
Pari-mutuel gambling and gaming machines, devices and accessories.
Pencils, mechanical (except functional parts and plating).
Pins (except safety pins, common pins, laundry net and laundry identification pins, or safety catches on products otherwise permitted under this order).
Pleasure boat fastenings and fittings.
Razors operated by electricity (except functional parts and parts for conducting electricity).
Razors not operated by electricity (except (1) in making safety razors: heads, functional parts for heads, and plating; and (2) in making straight razors: rivets, pins and washers).
Razor blade magazines.
Reflectors (except photographic and except as an undercoating or an overcoating in electroplating with silver or chromium).
Signs and advertising displays (except current-carrying parts).
Sporting goods and equipment (except fishing equipment and supplies for commercial fishing use, firearms, ammunition, and except reel gears, bearings and spools, swivels and snaps, rod mountings and copper for plating of baits and lures for sport fishing use).
Staplers and stapler machines (not including foot-operated or power-driven stitching machines).
Stationery supplies including but not limited to:
Desk accessories.
Office supplies.
Pencils (except for ferrules).
Pens and penholders.
Statues and statuettes (except religious and artists' originals).
Sundials.
*Tent poles and parts.
Tobacco pipes.
Toys (except in motors and essential operating parts).
Unions and union fittings (except seats, and except for other parts of unions and union fittings (1) where and to the extent that the physical and chemical properties of the liquid or gas passing through the union or union fittings make the use of any other material dangerous or impractical, or (2) where the valve is of a type designed for use in an air conditioning or refrigeration "system", or (3) where use of copper and tubing and/or brass pipe is permitted).
Umbrellas and parasols.
Vacuum bottles and jugs.
Valve handles (except plumbing fixture trim).
Walking sticks and canes.
Weather vanes.
Weight reducing and exercising machines (except for current-carrying parts).
Wool (except metal sponges intended for use in dairy products processing plants and by the canning industry and for filtering purposes).

## LIST B

(See section 7)

The use of the forms and products of copper defined in section 3 and of any component parts made therefrom in the items listed below (excluding repair parts) is prohibited except to the extent permitted in the order or the list: *Provided, however,* That such material may be used in such items included in the list as are marked with as asterisk in cases where such items are to be used by the armed forces of the United States, including the United States Coast Guard.

BUILDERS' HARDWARE

Protective brass plating of all listed items of builders' hardware is permitted where other types of finishes are not practicable.
Door knobs.
Letter slots.

BUILDING MATERIALS

Fac[illegible] fittings for [illegible]floor raceway systems.

Flashings (except (1) cap and base flashing for built-up roofing, (2) through-wall flashing in parapet walls, (3) flashing for chimneys, vent stacks and all other vertical surfaces rising through roof levels, (4) roof-to-side wall flashing, (5) valley flashing for slate, tile and cement shingle roofs, (6) door and window head flashing, (7) expansion joint flashing).
Gravel stops.
Shower pans.
Terrazzo strips.
Fins for: Unit heaters, unit ventilators, unit ventilator inlet wall boxes and convectors, and blast heating coils, or any apparatus using such coils as part of its construction.

CIVILIAN-TYPE MOTOR VEHICLE: PASSENGER AUTOMOBILES INCLUDING TAXICABS, STATION WAGONS, AMBULANCES, HEARSES, TRUCKS, TRUCK TRACTORS, TRUCK TRAILERS, MOTORCYCLES AND BUSSES.

Hubcaps (except for plating).
Radio antennae for vehicles.
Sidewalk or curbstone warning devices for automobiles.

CLOTHING AND DRESS ACCESSORIES, NOT INCLUDING SAFETY EQUIPMENT

*Slide fasteners (zippers) (except (1) for the following functional components: slider bodies, separating end-components and top and bottom stops; and (2) except for applications in safety garments, work clothing, rubber footwear, foundation and surgical garments were necessary for reasons of strength, launderability and anticorrosion).

FURNISHINGS AND EQUIPMENT

Refrigerator and water heater installation connections (except for high pressure LPG connections from tank to fixture).

FURNITURE AND FIXTURES

Fittings (except hospital and laboratory).

HARDWARE, MISCELLANEOUS

Tags for pets.

HOUSEHOLD ELECTRICAL APPLIANCES

(Except for operational parts where the properties supplied by the copper are essential or where necessary for electrical conductivity)

Coffee makers.
Home and farm freezers.
Ice cream freezers.
Waffle irons.

REFRIGERATION AND AIR CONDITIONING MACHINERY AND EQUIPMENT

(Commercial and Industrial)

(Except where copper products or copper-base alloy products are essential for the following: carbonators, complete condensing units less condensers, dehydrators, draft arms for soda fountain equipment, electrical controls and wiring, fittings, protective coatings, refrigerant circuits, refrigerant connections between compressor and cooling coils, refrigerant flow control valves, sight glasses, soldering and brazing materials, strainers, suction line heat exchangers, tube sheets, valves, water cooler low sides and pre-coolers, water flow control valves and water spray nozzles for evaporative condensers, evaporative coloers, and air washers)

Commercial and industrial refrigeration and air conditioning machinery and equipment including but not limited to:

Air conditioning systems, self-contained or remote.
Air washers.
Blast coolers.
Blast freezers.
Bottled beverage coolers.
Carbonated beverage dispensing systems (except coin operated).
Compressor stop valves (except valve seats, gaskets, bonnets, discs, disc screens, and protective coverings for valve stems).
Evaporative condensers.
Evaporative coolers (desert type).
Finned air-cooled condensers except those used for hermetic systems where the condenser is exposed to the outside air or for transportation systems.
Finned coils or evaporators.
Florist refrigerators.
Fountainettes.
Frozen food cabinets.
Ice cream cabinets.
Ice cube makers.
Malt beverage dispensing systems.
Mortuary refrigerators.
Non-carbonated beverage dispensing systems (except coin operated).
Packaged air conditioners (room, window, and store coolers).
Reach-in refrigerators.
Refrigerated display cases.
Refrigeration systems, self-contained or remote.
Reverse cycle heating and air conditioning systems (heat pumps).
Sandwich units.
Shell and tube or shell and coil condensers (except water courses, either straight or finned tube, where the refrigerant is in contact with the tube).
Shell and tube or shell and coil water chillers (except water courses, either straight or finned tube, where the refrigerant is in contact with the tube).
Soda fountains.
Space coolers.
Unit coolers.
Walk-in refrigerators.
Water coolers (except bubblers, bubbler connections, faucets and faucet connections).

MISCELLANEOUS

Ball point pens (except necessary operational parts).
Dehumidifiers for home and office use (except operational parts where the properties supplied by the copper are essential or where necessary for electrical conductivity).
Flashlight cases (except contact points for carrying current).
Garment hangers.
Hollow ware (except for hotels, restaurants, institutions and ecclesiastical use).
Identification and directional signs (except current-carrying parts).
Key chains and catches and fasteners therefor.
Lawn sprinklers (except working parts and propellers).
Outboard motors (except for operational parts).
Portable electric lanterns, such as railroad, miners' and industrial (except parts for conducting electricity and for plating).
Shells and caps for sockets.
Ties (except for explosives and other products where the properties supplied by copper are essential).

[F. R. Doc. 51-3284; Filed, Mar. 9, 1951; 5:06 p. m.]

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[NPA Order M-48]

## M-48—BISMUTH

This order is found necessary and appropriate to promote the national defense and is issued pursuant to the Defense Production Act of 1950. In the formulation of this order there has been consultation with industry representatives, including trade association representatives, and consideration has been given to their recommendations. However, consultation with representatives of all trades and industries affected in advance of the issuance of this order has been rendered impracticable due to the necessity for immediate action, and because the order affects a large number of different trades and industries.

Sec.
1. What this order does.
2. Definitions.
3. Limitations on use of bismuth and bismuth alloys.
4. Limitations on acceptance of rated orders.
5. Set aside from production and imports.
6. Limitations on acceptance of delivery.
7. Application for delivery from set aside reserve.
8. Certification.
9. Inventories.
10. Records and reports.
11. Application for adjustment.
12. Communications.
13. Violations.

AUTHORITY: Sections 1 to 13 issued under sec. 704, Pub. Law 774, 81st Cong. Interpret or apply sec. 101, Pub. Law 774, 81st Cong.; sec. 101, E. O. 10161, Sept. 9, 1950, 15 F. R. 6105, 3 CFR, 1950 Supp., sec. 2, E. O. 10200, Jan. 3, 1951, 16 F. R. 61.

SECTION 1. *What this order does.* The purpose of this order is to set forth the conditions under which bismuth and bismuth alloys may be delivered and accepted, and the processes and products in which these materials can be used. This order also establishes limitations on the acceptance of rated orders, and on inventories of bismuth, bismuth alloys and articles made therefrom. It explains the conditions under which reports are required in connection with the production, distribution, importation, use and inventories of these materials. It is the intent of this order that other materials which are not in short supply will be substituted for bismuth wherever possible.

SEC. 2. *Definitions.* As used in this order:

(a) "Person" means any individual, corporation, partnership, association or any other organized group of persons and includes any agency of the United States or any other government.

(b) "Base period" means the six months' period ending June 30, 1950.

(c) "Bismuth" means metallic bismuth in bars, ingots, pigs, sticks, slabs, kegs, moss powder or other shapes or forms suitable for use in the manufacture of industrial or medicinal products or bismuth alloys.

(d) "Bismuth alloy" means any alloy containing more than 1 percent bismuth.

(e) "Bismuth product" means any semi-finished or finished article containing bismuth commercially recognized.

(f) "Scrap" means all materials or objects which are the waste or by-product of industrial fabrications or processes, or which have been discarded for obsolescence, failure or other reason, including, but not limited to, items such as unused, discarded or broken tools, dies, or accessories for production equipment which have been unused for a period in excess of six months, and which contain bismuth commercially recoverable.

(g) "Producer" means any person producing bismuth or bismuth alloys for re-

sale, and any person having bismuth or bismuth alloys produced for him under toll agreement.

(h) "Dealer" means any person who receives physical deliveries of bismuth, bismuth alloys or bismuth products and sells or holds same for resale without change in form.

(i) "Import" means to transport in any manner into the continental United States from areas outside the continental United States, including territories and possessions. It includes shipments into foreign-trade zones, customs bonded warehouses, and customs custody, except when such shipments are merely in transit through the continental United States, to destinations outside the continental United States, as shown by the bills of lading or other shipping documents. However, if any such material in transit is halted or diverted to a destination in the continental United States or subjected to processing or manufacture in the continental United States, it becomes an "import" for the purposes of this order.

SEC. 3. *Limitations on use of bismuth and bismuth alloys.* (a) Unless specifically authorized by the National Production Authority, commencing on April 1, 1951, no person shall put into process or otherwise use any bismuth or bismuth alloys in the manufacture, treatment, installation, or construction of any item or product, or in any process, or for any purpose, except those set forth in the Schedule appearing at the end of this order and to the extent permitted thereby. Uses not thus expressly authorized are prohibited.

(b) Paragraph (a) of this section does not prohibit the completion and subsequent sale of any items or the completion of any processes or installations if the manufacturing, processing, or installation was begun on or before April 1, 1951, and if such manufacturing, processing or installation is completed not later than April 30, 1951.

SEC. 4. *Limitations on acceptance of rated orders.* Notwithstanding the provisions of NPA Reg. 2 and unless otherwise directed by the National Production Authority:

(a) No producer shall be required to accept rated orders for shipment in any one month for a total weight of bismuth, bismuth alloys and bismuth products in excess of 50 percent of his scheduled production of such items, in terms of bismuth content, during that month.

(b) No dealer shall be required to accept rated orders for shipment in any one month for a total weight of bismuth, bismuth alloys and bismuth products in excess of 25 percent of the total quantity of bismuth, bismuth alloys and bismuth products available to him, in terms of bismuth content, during that month.

SEC. 5. *Set aside from production and imports.* In addition to the requirements of section 4 of this order, commencing on April 1, 1951:

(a) Each producer shall set aside a reserve of 20 percent of his monthly production of bismuth (including bismuth produced for him by others under toll agreement, but not bismuth which he produces for others under toll agreement). Except as otherwise directed by the National Production Authority, this reserve may be delivered only upon the specific authorization of the National Production Authority in accordance with the procedure stated in section 7 of this order.

(b) Any person who imports bismuth shall set aside in each month a reserve of 20 percent of his imports of bismuth during such month. Except as otherwise directed by the National Production Authority, this reserve may be delivered only upon the specific authorization of the National Production Authority in accordance with the procedure stated in section 7 of this order.

SEC. 6. *Limitations on acceptance of delivery.* Except as may be authorized in accordance with the procedure stated in section 7 of this order and subject to the inventory limitations contained in section 9 of this order, no person shall accept delivery from domestic sources in any month of a total quantity by weight of bismuth and bismuth alloys (bismuth content), in excess of 60 percent of his average monthly receipts of such materials (bismuth content), during the base period, or 100 pounds, whichever is greater.

SEC. 7. *Application for delivery from set aside reserve.* Any person who, in the public interest, considers that he requires more bismuth than he can obtain from commercial sources, may apply to the National Production Authority for a delivery of bismuth from the set aside. Such application shall be submitted by letter not later than the 25th day of the month preceding the month during which delivery is desired, and shall set forth: the quantity of bismuth desired, the public interest which will be served, the desired delivery date, the applicant's anticipated receipts of non-set aside bismuth, the applicant's anticipated inventory of bismuth at the beginning of the month during which bismuth from the set aside is desired, and such other facts as may be pertinent. If the request is approved, the applicant will be notified that a particular supplier has been directed to make delivery of the bismuth concerned, and that the applicant is thereby authorized to accept delivery of this additional quantity of bismuth for a specified use.

SEC. 8. *Certification.* (a) Commencing on April 1, 1951, no person shall sell or deliver, and no person shall purchase or accept delivery of, any bismuth or bismuth alloys unless the purchaser furnishes a signed certification as follows:

> The undersigned certifies, subject to statutory penalties, that acceptance of delivery of the bismuth or bismuth alloys herein ordered is permitted by NPA Order M-48, and this material will be used only for the purposes permitted thereby, as follows: _____
> Specify end use

This certification constitutes a representation by the purchaser to the seller and to the National Production Authority that the bismuth or bismuth alloys delivered will be used only for the purpose or purposes set forth in the appended Schedule, that such use is not prohibited by other applicable orders or regulations of the National Production Authority, and that the receipt is in accordance with sections 6 and 9 of this order.

(b) This certification shall not be required in connection with: (1) The delivery of bismuth to the General Services Administration for the stockpile of strategic materials, (2) the delivery of bismuth or bismuth alloys pursuant to a specific authorization of the National Production Authority, or (3) the importation of bismuth or bismuth alloys.

SEC. 9. *Inventories.* (a) No person shall receive or accept delivery of a quantity of bismuth, bismuth alloys, bismuth products or scrap if his inventory of such material is, or by such receipt would become, more than the smallest quantity of such material which he reasonably requires to meet his deliveries or maintain his scheduled rate of operations during the next succeeding 30-day period, or in excess of a "practicable minimum working inventory" as defined in NPA Reg. 1, whichever is less.

(b) Except as otherwise provided by this section, NPA Reg. 1 (particularly § 10.11 *Imported Materials*) will apply to all materials mentioned in paragraph (a) of this section.

SEC. 10. *Records and reports.* (a) Any person who on any day of any month has in his possession or under his control a quantity of bismuth in excess of 100 pounds or who receives, uses or ships a quantity of bismuth in excess of 100 pounds during any month, shall complete and file Form NPAF-40 on or before the 30th day of March 1951 with respect to February 1951, and on the 15th day of each succeeding month with respect to such transactions, possession or use during the preceding month.

(b) Producers and importers of bismuth shall report by letter not later than March 20, 1951 with respect to April 1951, and not later than the 20th day of each month thereafter, the quantity of bismuth which they expect to set aside during the next succeeding month in accordance with section 5 of this order.

(c) The reports required by this section shall be filed with the National Production Authority, Washington 25, D. C.

(d) Each person participating in any transaction covered by this order shall retain in his possession for at least two years records of receipts, deliveries, inventories, production and use, in sufficient detail to permit an audit that determines for each transaction that the provisions of this order have been met. This does not specify any particular accounting method and does not require alteration of the system of records customarily maintained, provided such records supply an adequate basis for audit. Records may be retained in the form of microfilm or other photographic copies instead of the originals.

(e) All records required by this order shall be made available at the usual place of business where maintained for inspection and audit by duly authorized representatives of the National Production Authority.

(f) Persons subject to this order shall make such records and submit such

other reports to the National Production Authority as it shall require subject to the terms of the Federal Reports Act (Pub. Law 831, 77th Cong., 5 U. S. C. 139–139F).

SEC. 11. *Application for adjustment.* Any person affected by any provision of this order may file a request for adjustment or exception upon the ground that his business operation was commenced during or after the base period, or because any provision otherwise works an undue or exceptional hardship upon him not suffered generally by others in the same trade or industry, or that its enforcement against him would not be in the interest of the national defense or in the public interest. In considering requests for adjustment which claim that the public interest is prejudiced by the application of any provision of this order, consideration will be given to the requirements of public health and safety, civilian defense, and dislocation of labor and resulting unemployment that would impair the defense program. Each such request shall be in writing and shall set forth all pertinent facts, the nature of the relief sought and the justification therefor.

SEC. 12. *Communications.* All communications concerning this order shall be addressed to the National Production Authority, Washington 25, D. C., Ref: M–48.

SEC. 13. *Violations.* Any person who wilfully violates any provision of this order or any other order or regulation of the National Production Authority or wilfully conceals a material fact or furnishes false information in the course of operation under this order is guilty of a crime and, upon conviction, may be punished by fine or imprisonment or both. In addition, administrative action may be taken against any such person to suspend his privilege of making or receiving further deliveries of materials or using facilities under priority or allocation control and to deprive him of further priorities assistance.

NOTE: All reporting and record-keeping requirements of this order have been approved by the Bureau of the Budget in accordance with the Federal Reports Act of 1942.

This order shall take effect, except as otherwise specifically stated, on March 9, 1951.

NATIONAL PRODUCTION AUTHORITY,
[SEAL] MANLY FLEISCHMANN,
*Administrator.*

SCHEDULE OF PERMITTED USES

[See Section 3]

The use of bismuth and bismuth alloys is permitted only for the following items, processes and purposes:

(a) Anchoring:

1. Bearings, bushings and parts in machinery.
2. Bushings in drill jigs.
3. Inserts and ceramics, plastics, etc.
4. Location members, pads and points in aircraft and automotive assembly, drill, inspection and welding fixtures.
5. Pole pieces in magnetic chucks and fixtures.
6. Precision parts for machining, testing and inspection.
7. Punches and dies for blanking, piercing and trimming.
8. Repairing broken dies.
9. Shafts in rotors of alnico, etc.

(b) Making chucks for:

1. Well drill cores.
2. Holding irregular shapes for machining (split jaw).

(c) Making cores for:

1. Electroforming.
2. Intricate compound foundry cores.

(d) Making dies and punches for:

1. Sheet metal embossing and short run forming.
2. Form blocks for bending, forming and stretch press forming.

(e) Models and patterns for:

1. Dental and medical models and prosthetic devices.
2. Core dryer patterns.
3. Pantograph and Keller tracer models.
4. Master patterns for match plates.
5. "Lost Wax" patterns, precision castings.

(f) Molds for:

1. Duplicating plaster and plastic patterns.
2. Casting and forming plastics and plaster.
3. Holding irregular shaped parts.

(g) Production tooling:

1. Duplicate patterns for ceramics, plastics, pottery, etc.
2. Fixtures for assembly checking, die spotting, drilling, inspection.
3. Filler for mold and tube bending and for fabricating seamless fittings.
4. Hold-down clamp pads.
5. Masks for electroforming and spray painting.
6. Nests for drill jigs and dial feed stations.
7. Shimming pads in aircraft tooling fixtures.
8. Supporting parts while machining and grinding.
9. Repairing wood, plastic, masonite and plastic tooling.
10. Stripper plates in stamping dies.
11. Trim dies for die casting and plastics.

(h) Miscellaneous:

1. Filling blowholes and defects in castings.
2. Fusible elements in sprinkler head links, protective and safety equipment.
3. Heat and/or transfer and pressure medium in autoclave, textile dyeing and drying equipment and constant temperature heat treating baths.
4. Liquid seals for bright annealing nitriding furnaces.
5. Low temperature solders in delicate assemblies, instruments, ammunition, etc.
6. Proof casting, forging dies, molds, gun chambers, etc.
7. Sealing adjustment screws on instruments, torque wrenches, etc.
8. Hermetic and vacuum seals—glass and metal.
9. Selenium rectifiers.
10. Shielding—X-ray equipment and therapeutic short wave equipment.
11. Low melting solders for ammunition boxes, shell cases, fuse sealing, etc.

(i) To comply with safety regulations issued under governmental authority which require the use of bismuth as a fusible alloy for protective devices.

(j) In research laboratories where and to the extent that the physical or chemical material requirements make the use of any other material impracticable.

(k) As an alloying material in the production of aluminum, stainless steels and malleable iron and cast iron to the extent necessary to improve machinability.

(l) To make bismuth salts used in pharmaceutical preparations.

[F. R. Doc. 51–3285; Filed, Mar. 9, 1951; 5:06 p. m.]

# TITLE 39—POSTAL SERVICE

## Chapter I—Post Office Department

PART 127—INTERNATIONAL POSTAL SERVICE: POSTAGE RATES, SERVICE AVAILABLE, AND INSTRUCTIONS FOR MAILING

MEXICO

Whereas the Post Office Department has received advice through the Department of Commerce that certain import restrictions have been relaxed by the Mexican Government, and it having been found that compliance with the notice, public rule making procedure, and effective date requirements of the Administrative Procedure Act (5 U. S. C. 1003) is impracticable for the reason that such compliance would impede the due and timely execution of the functions of this Department:

Now, therefore, it is ordered, that, effective at once, Part 127 (39 CFR Part 127) be amended as follows:

In § 127.304 *Mexico* amend paragraph (b) (9) to read as follows:

(b) *Parcel post.* * * *

(9) *Prohibitions.*—(i) *Import permits.* A large variety of items require import permits to be obtained by the addressees in Mexico, when the value of the shipment is 100 Mexican pesos or over. Information as to what articles require import licenses, and as to rates of Mexican customs duty, may be obtained from the American Republics Division, Office of International Trade, Department of Commerce, Washington 25, D. C., or from any regional or district office of that Department.

(ii) *For sanitary reasons.* Pacifiers for the amusement of babies. For medicines, cosmetics, and toilet articles, see paragraph (a) *Regular mails* of this section. The customs service requires, from persons receiving by mail from abroad, in small quantities, products of animal origin contained in tin cans, a certificate of sanitary inspection issued by the Department of Agriculture and Fomento. However, the products in question may be exempted from the above-mentioned inspection certificate when their weight is less than 11 pounds.

(iii) *For the protection of animals and plants.* (*a*) Certain plants and plant products are prohibited from importation or are admitted under restrictions. Interested patrons may be informed that information can be obtained from the Bureau of Entomology and Plant Quarantine, Department of Agriculture, Washington 25, D. C., or from one of the offices of that Bureau located at principal ports of entry.

(*b*) Parasites and predators of injurious insects, unless intended for the control of those insects and exchanged between officially recognized institutions.

(iv) *Arms, etc.* Arms require the special permission of the Secretariat of War and Navy. The importation by mail of pistols, hunting and target arms, requires also a certificate from the Mexican consul at the place of shipment. Pistols and other instruments for the projection of tear gas are prohibited.

(v) *For other reasons.* Works violating the Mexican copyright laws. Bank notes, coins of all kinds, and values payable to bearer. As an exception, the Bank of Mexico and the banks associated therewith are authorized to import bank notes exclusively for the purpose of exchange. Uncanceled postage stamps are accepted only under registration.

(R. S. 161, 396, secs. 304, 309, 42 Stat. 24, 25; 5 U. S. C. 22, 369; and the terms of postal conventions and agreements entered into pursuant to R. S. 398, 48 Stat. 943; 5 U. S. C. 372)

[SEAL] V. C. BURKE,
*Acting Postmaster General.*

[F. R. Doc. 51-3191; Filed, Mar. 12, 1951; 8:45 a. m.]

# PROPOSED RULE MAKING

## DEPARTMENT OF AGRICULTURE

### Production and Marketing Administration

### [ 7 CFR, Part 70 ]

GRADING AND INSPECTION OF POULTRY AND EDIBLE PRODUCTS THEREOF; UNITED STATES SPECIFICATIONS FOR CLASSES, STANDARDS, AND GRADES WITH RESPECT THERETO

NOTICE OF PROPOSED RULE MAKING

Notice is hereby given that the United States Department of Agriculture is considering the issuance, as hereinafter proposed, of revised rules governing the grading and inspection of poultry and edible products thereof and United States specifications for classes, standards, and grades with respect thereto, to become effective May 1, 1951, pursuant to the authority contained in the Agricultural Marketing Act of 1946 (60 Stat. 1087; 7 U. S. C. 1621 et seq.) and the Department of Agriculture Appropriation Act 1951 (Pub. Law 759), 81st Cong., approved September 6, 1950). The proposed rules will supersede the currently effective Part 70 (7 CFR Part 70), insofar as applicable to poultry and edible products thereof, since such part is comprised of rules and specifications governing grading and inspection of both poultry and domestic rabbits. It is planned to revise the rules and specifications for domestic rabbits and, therefore, no references to domestic rabbits are contained in the proposals set forth herein. The proposed revision with respect to domestic rabbits will be published in the FEDERAL REGISTER and the industry will be given an opportunity to submit relevant written data, views, or arguments. It is planned to make the revised rabbit regulations and the revised poultry regulations effective at the same time.

Most of the provisions of the proposed rules and specifications have received thorough consideration throughout the country at numerous conferences held with industry and college and State departments of agriculture representatives. Among other things, the proposed revision of the rules and specifications changes the provisions governing the grading of ready-to-cook poultry by requiring, as a prerequisite thereto, some form of official inspection for wholesomeness.

All persons who desire to submit written data, views, or arguments in connection with the proposals should file the same in triplicate with the Chief of the Marketing Services Division, Poultry Branch, Production and Marketing Administration, United States Department of Agriculture, Room 2099 South Building, Washington 25, D. C., not later than the close of business on the 30th day after publication of this notice in the FEDERAL REGISTER.

The proposed rules and specifications are as follows:

SUBPART A—RULES GOVERNING THE GRADING AND INSPECTION OF POULTRY AND EDIBLE PRODUCTS THEREOF

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70.8 Other applicable regulations.
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70.11 Identifying and marketing products.
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70.14 Prerequisites to grading and inspection.
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70.16 Time of grading or inspection in an official plant.
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INSPECTION

70.19 Manner of handling products in an official plant.
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70.25 Reinspection of edible products.
70.26 Edible products for canning.
70.27 Products contaminated by polluted water; procedure for handling.
70.28 Preparation of animal food or similar uninspected articles in an official plant.
70.29 Appeal inspections; how made.
70.30 Inspection certificates; issuance and disposition.

GRADING

70.31 General.
70.32 Live poultry.
70.33 Dressed poultry and ready-to-cook poultry.
70.34 Basis of acceptability of other official inspection systems.
70.35 Certificates.
70.36 Application for regrading of a graded product; regrading certificates.
70.37 Appeal grading.
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SANITARY REQUIREMENTS

70.39 Minimum standards for sanitation, facilities, and operating procedures in official plants.
70.40 Authority of Administrator to amend minimum standards for sanitation, facilities, and operating procedures in official plants.

SUBPART B—UNITED STATES SPECIFICATIONS FOR CLASSES, STANDARDS, AND GRADES OF POULTRY AND EDIBLE PRODUCTS THEREOF

70.101 United States specifications for kinds and classes of live poultry, dressed poultry, and ready-to-cook poultry.
70.102 United States specifications for standards of quality for live poultry on an individual bird basis.
70.103 United States specifications for standards of grades for live poultry.
70.104 United States specifications for standards of quality for individual carcasses of dressed poultry and ready-to-cook poultry.
70.105 United States specifications for standards of grades for dressed poultry and ready-to-cook poultry.

SUBPART A—GRADING AND INSPECTION OF POULTRY AND EDIBLE PRODUCTS THEREOF

DEFINITIONS

§ 70.1 *Definitions.* Unless the context otherwise requires, the following terms shall have the following meaning:

(a) "Act" means the following provisions of the Agricultural Marketing Act of 1946 (60 Stat. 1087; 7 U. S. C. 1621 et seq.) and the Department of Agriculture Appropriation Act of 1951 (Pub. Law 759, 81st. Cong.) or any other act of Congress conferring like authority:

AGRICULTURAL MARKETING ACT OF 1946

* * * to develop and improve standards of quality, condition, quantity, grade, and packaging, and recommend and demonstrate such standards in order to encourage uniformity and consistency in commercial practices * * *

To inspect, certify, and identify the class, quality, quantity, and condition of agricultural products when shipped or received in interstate commerce under such rules and regulations as the Secretary of Agriculture may prescribe, including assessment and collection of such fees as will be reasonable and as nearly as may be to cover the cost of the service rendered, to the end that agricultural products may be marketed to the best advantage, that trading may be facilitated, and that consumers may be able to obtain the quality products which they desire, * * *

DEPARTMENT OF AGRICULTURE APPROPRIATION ACT, 1951

* * * Market inspection of farm products: For the investigation and certification, in one or more jurisdictions, to shippers and other interested parties of the class, quality,

and condition of any agricultural commodity or food product, whether raw, dried, canned, or otherwise processed, and any product containing an agricultural commodity or derivative thereof when offered for interstate shipment or when received at such important central markets as the Secretary may from time to time designate, or at points which may be conveniently reached therefrom under such rules and regulations as he may prescribe, including payment of such fees as will be reasonable and as nearly as may be to cover the cost for the service rendered. * * *

Marketing farm products: For acquiring and diffusing among the people of the United States useful information relative to the needed supplies, standardization, classification, grading, preparation for market, handling, transportation, storage, and marketing of farm and food products, including the demonstration and promotion of the use of uniform standards of classification of American farm and food products throughout the world, * * *

(b) "Administration" means the Production and Marketing Administration of the Department.

(c) "Administrator" means the Administrator of the Production and Marketing Administration of the Department, or any other officer or employee of the Department to whom there has heretofore been delegated, or to whom there may hereafter be delegated, the authority to act in his stead.

(d) "Applicant" means any interested party who requests any inspection service or grading service.

(e) "Carcass" means any poultry carcass.

(f) "Circuit Supervisor" means the officer in charge of the poultry inspection service in a circuit consisting of a group of stations within an area.

(g) "Class" means any subdivision of a product based on essential physical characteristics that differentiate between major groups of the same kind or between species.

(h) "Condition" means any condition, including but not being limited to, the state of preservation, cleanliness, or soundness of any product; or any condition, including but not limited to, the processing, handling, or packaging which affects such product.

(i) "Condition and wholesomeness" means the condition of any product and its healthfulness and fitness for human food.

(j) "Department" means the United States Department of Agriculture.

(k) "Dressed poultry" means poultry which has been slaughtered for human food with head, feet, and viscera intact and from which the blood and feathers have been removed.

(l) "Edible poultry byproduct" means any giblets or any edible part of dressed poultry other than eviscerated poultry.

(m) "Edible product" means any product other than live poultry and dressed poultry.

(n) "Eviscerated poultry" means any dressed poultry from which the pinfeathers, vestigial feathers (hair or down, as the case may be), head, shanks, crop, oil gland, trachea, esophagus, entrails, reproductive organs, and lungs have been removed and, with or without the giblets, is ready to cook without need of further processing.

(o) "Food product containing poultry product" means any article of food for human consumption which is prepared in part from any edible portion of dressed poultry or from any product derived wholly from such edible portion, if such edible portion or product does not comprise a substantial portion of such article of food.

(p) "Giblets" means the liver from which the bile sac has been removed, the heart from which the pericardial sac has been removed, and the gizzard from which the lining and contents have been removed: *Provided*, That each such organ has been properly trimmed and washed.

(q) "Grader" means any employee of the Department authorized by the Secretary, or any other individual to whom a license has been issued by the Secretary, to investigate and certify, in accordance with the regulations in this part, the class, quality, quantity, and condition of products.

(r) "Grading" or "grading service" means (1) the act whereby a grader determines, according to the regulations in this part, the class, quality, quantity, or condition of any product by examining each unit thereof, or each unit of the representative sample thereof drawn by a grader, and issues a grading certificate with respect thereto; (2) in addition to the foregoing, the act whereby the grader identifies, according to the regulations in this part, the graded product; (3) with respect to an official plant, the act whereby a grader determines that the products in such plant are processed, handled, and packaged in accordance with § 70.39; and (4) any regrading or any appeal grading of a previously graded product.

(s) "Grading certificate" means a statement, either written or printed, issued by a grader, pursuant to the regulations in this part, relative to the class, quality, quantity, or condition of a product.

(t) "Identify" means to apply official identification to products or the containers thereof.

(u) "Inspected and certified" or "certified" means, with respect to any product, that it has undergone an inspection and was found, at the time of such inspection, to be sound, wholesome, and fit for human food.

(v) "Inspected," "inspection service," or "inspection of products for condition and wholesomeness" means any inspection by an inspector to determine, in accordance with regulations in this part, (1) the condition and wholesomeness of dressed poultry, or (2) the condition and wholesomeness of any edible product at any stage of the preparation or packaging thereof in the official plant where inspected and certified, or (3) the condition and wholesomeness of any previously inspected and certified product if such product has not lost its identity as an inspected and certified product. In addition to the foregoing, the terms "inspection" and "inspection service" shall each mean any inspection by an inspector to determine, in accordance with the regulations in this part, the condition of dressed poultry as it applies to the processing, handling or packaging of such product.

(w) "Inspection certificate" means a statement, either written or printed, issued by an inspector, pursuant to the regulations in this part, relative to the condition and wholesomeness of products.

(x) "Inspector" means any person who is licensed by the Secretary to investigate and certify in accordance with the regulations in this part, the condition and wholesomeness of products or in the condition of dressed poultry. An inspector is an employee of the Department or of a State; he may be a graduate veterinarian or a layman.

(y) "Interested party" means any person financially interested in a transaction involving any inspection or grading.

(z) "National supervisor" means (1) the officer in charge of the poultry inspection service of the Administration, (2) the officer in charge of the poultry grading service of the Administration, and (3) such other officers or employees of the Department who may be so designated by the officer in charge of the poultry inspection and grading service of the Administration.

(aa) "Office of grading" means the office of any grader.

(bb) "Official identification" means the symbol represented by a stamp, label, seal, or other device approved by the Administrator and affixed to any product, or to any container thereof, stating that the product was inspected or graded or both; and the class, quality, or condition of such product as determined by a grader may be indicated.

(cc) "Official plant" means one or more buildings, or parts thereof, comprising a single plant in which the facilities and methods of operation therein have been approved by the Administrator as suitable and adequate for operation under inspection or grading service and in which inspection or grading is carried on in accordance with the regulations in this part.

(dd) "Person" means any individual, partnership, association, business trust, corporation, or any organized group of persons, whether incorporated or not.

(ee) "Poultry" means any kind of domesticated bird, including, but not being limited to, chickens, turkeys, ducks, geese, pigeons, and guineas.

(ff) "Poultry food product" means any article of human food or any article intended for or capable of being so used which is prepared or derived in whole or in substantial part, from any edible portion of dressed poultry.

(gg) "Poultry grading and inspection service" means the personnel of the Administration who are actively engaged in the administration, application and direction of poultry grading and inspection programs and services pursuant to the regulations in this part.

(hh) "Product" means each of the following: (1) Dressed poultry; (2) eviscerated poultry; (3) edible poultry byproduct; (4) poultry food product; and (5) with respect to grading service only, live poultry.

(ii) "Quality" means the inherent properties of any product which determine its relative degree of excellence.

(jj) "Ready-to-cook poultry" means any eviscerated poultry or any cut-up or disjointed portion thereof.

(kk) "Regional supervisor" means any employee of the Department in charge of poultry grading service or poultry inspection service in a designated geographical area.

(ll) "Regulations" means the provisions of this entire part and such United States specifications for classes, standards, and grades for products as may be in effect at the time grading or inspection is performed.

(mm) "Secretary" means the Secretary of the Department, or any other officer or employee of the Department to whom there has heretofore been delegated or to whom there may hereafter be delegated, the authority to act in his stead.

(nn) "Soundness" means freedom from external evidence of any disease or condition which may render a carcass unfit for food.

(oo) "State supervisor" means any authorized and designated individual who is in charge of the poultry grading service or the poultry inspection service in a State. A State supervisor of poultry inspection service shall be a veterinarian and he may be either a Federal-State employee or a Federal employee.

(pp) "Station supervisor" means any authorized individual who is designated to supervise the poultry grading service or the poultry inspection service in a large official plant or in a group of several smaller plants.

ADMINISTRATION

§ 70.2 *Administration.* The Administrator shall perform for and under the supervision of the Secretary, such duties as are prescribed in the regulations in this part and as the Secretary may require in the administration of the regulations in this part.

GENERAL

§ 70.3 *Grading and inspection programs and services*—(a) *Kinds of services.* The regulations in this part provide for the following kinds of service with respect to live, dressed, and ready-to-cook poultry:

(1) *Grading of live poultry.*

(2) *Grading of dressed poultry.* (i) In an official plant.

(ii) At terminal markets and other receiving points other than official plants.

(3) *Grading of ready-to-cook poultry.* (i) In an official plant.

(ii) At terminal markets and other receiving points other than official plants.

(4) *Inspection of dressed poultry in official plants for processing as ready-to-cook poultry.*

(5) *Inspection in an official plant of ready-to-cook poultry for canning or poultry to be prepared as edible products other than eviscerated poultry.*

(6) *Certification of dressed poultry produced under sanitary requirements; in official plants.* With respect to any official plant, dressed poultry as such, may be certified by a grader as having been processed, handled and packed in accordance with the minimum standards for sanitation, facilities, and operating procedures in official plants. However, in official plants which have available the services of an inspector who is authorized to inspect for condition and wholesomeness, such inspector is also authorized to certify dressed poultry, as such, as having been processed, handled, and packed in accordance with the minimum standards for sanitation, facilities, and operating procedures in official plants. The bulk containers of such dressed poultry which has been certified as aforesaid, shall be marked for identification purposes and appropriate grading or inspection processing reports shall be issued with respect thereto as required by the regulations in this part. In official plants where this kind of service is rendered all of the poultry that is processed in such official plant as dressed poultry shall be prepared in accordance with the regulations in this part and under the supervision of a grader or inspector.

(b) *Dressed poultry to be eligible for inspection or grading service shall have been processed in official plants.* Except as otherwise provided in this part, and as may be approved by the Administrator for a specified limited period with respect to dressed poultry which is to be inspected for canning, only dressed poultry which was processed in official plants in accordance with the regulations in this part may be graded or inspected and only dressed poultry from an official plant may be brought into another official plant. However, with respect to dressed poultry which was processed on the farm where it was raised, such poultry may be brought into official plants for grading or inspection, provided such poultry was dressed under sanitary conditions in accordance with such methods and operating procedures which are acceptable to the Administrator.

(c) *Inspection required during eviscerating operations at official plants under inspection service.* Any dressed poultry that is eviscerated in an official plant where inspection service is maintained, shall be inspected for condition and wholesomeness and no uninspected edible products shall be brought into such official plant.

(d) *Basis of service.* (1) Any inspection service in accordance with the regulations in this part shall be for condition and wholesomeness but, with respect to dressed poultry, as such, the inspection may be for condition only.

(2) Any grading service in accordance with the regulations in this part shall be for class, quality, quantity, or condition or any combination thereof. Grading service with respect to determination of quality of products shall be on the basis of United States specifications for classes, standards, and grades as contained in Subpart B of the regulations in this part. However, grading service may be rendered with respect to products which are bought and sold on the basis of institutional contract specifications and such service when approved by the Administrator, shall be rendered on the basis of the specifications of such contract.

(3) All grading service and all inspection service shall be subject to supervision at all times by the applicable station supervisor, State supervisor, circuit supervisor, regional supervisor, and national supervisor. Such services shall be rendered where the facilities and conditions are satisfactory for the conduct of the service and the requisite graders and inspectors are available.

(e) *Licensed graders and inspectors.* (1) Any person who is a Federal or State employee possessing proper qualifications as determined by an examination for competency, and who is to perform grading service or inspection service may be licensed by the Secretary as a grader or an inspector.

(2) Any prospective grader, other than a Federal or State employee, possessing proper qualifications as determined by an examination for competency and who is to perform grading service may be licensed by the Secretary as a grader.

(3) Any prospective grader, other than a Federal or a State employee, shall, prior to granting of the license, procure and deliver to the Administration a surety bond, issued by such surety as may be approved by the Administrator, in the amount of $1,000 for the proper performance of the duties of such licensee under the regulations in this part.

(4) All licenses issued by the Secretary shall be countersigned by the officer in charge of the poultry grading and inspection service of the Administration or any other designated official of such service.

(f) *Suspension of license or authority; revocation.* Pending final action by the Secretary, the officer in charge of the poultry grading and inspection service may, whenever he deems such action necessary, suspend any license or authority effective pursuant to the regulations in this part, by giving notice of such suspension to the respective individual involved, accompanied by a statement of the reasons therefor. Within seven days after the receipt of the aforesaid notice and statement of reasons by such individual, he may file an appeal, in writing, with the Secretary supported by any argument or evidence that he may wish to offer as to why his license or authority should not be suspended or revoked. After the expiration of the aforesaid seven-day period and consideration of such argument and evidence, the Secretary will take such action as he deems appropriate with respect to such suspension or revocation. When no appeal is filed within the prescribed seven days the license is revoked.

(g) *Surrender of license.* Each license which is suspended, or revoked, or has expired shall promptly be surrendered by the licensee to his immediate superior. Upon termination of the services of a licensed grader or inspector the licensee shall promptly surrender his license to his immediate superior.

(h) *Identification.* Each grader and inspector shall have in his possession at all times, and present upon request while on duty, the means of identification furnished by the Department to such person.

(i) *Financial interest of inspectors.* No inspector shall inspect any product in which he is financially interested.

§ 70.4 *Application for grading service or inspection service—*(a) *Who may obtain grading service or inspection service.* An application for grading service or inspection service may be made by any interested person, including, but not being limited to, the United States, any State, county, municipality, or common carrier, and any authorized agent of the foregoing.

(b) *How application may be made.* (1) Any application for inspection service must be made in writing and filed with the Administrator.

(2) An application for grading service to be rendered in an official plant must be made in writing and filed with the Administrator.

(3) An application for any grading service to be rendered other than in an official plant may be made in any office of grading, or with any grader at or nearest the place where the service is desired. Such application may be made orally, in writing, or by telegraph. If the application for grading service is made orally, the office of grading or the grader with whom the application is made, or the Administrator may require that the application be confirmed in writing.

(4) Each application for grading service or inspection service shall include such information as may be required by the Administrator in regard to the products and premises where the service is to be rendered.

(c) *Filing of application.* An application for grading service or inspection service shall be regarded as filed only when made pursuant to the regulations in this part.

(d) *Authority of applicant.* Proof of the authority of any person applying for grading service or inspection service may be required at the discretion of the Administrator.

(e) *Application for inspection service or grading service in official plants; approval.* Any person desiring to process and pack products in a plant under grading service or inspection service, or both, must receive approval of such plant and facilities as an official plant prior to the rendition of such service. Application for continuous grading service in an official plant other than the service provided in § 70.3 (a) (6) may be approved only when a substantial majority (approximately 75 percent) of the product processed each month is graded for quality and packed according to grade. An application for grading service or inspection service to be rendered in an official plant shall be approved according to the following procedure:

(1) *Initial survey.* When an application has been filed for grading service or inspection service, as aforesaid, the regional supervisor, or his assistant, shall examine the plant, premises, and facilities and shall specify any additional or necessary facilities required for the service. Appeals with respect to any such specification may be made to the national supervisor.

(2) *Drawings and specifications to be furnished in advance of construction or alterations.* Four copies of drawings, consisting of floor plans of space to be included in the official plant, showing the locations of such features as the principal pieces of equipment, floor drains, principal drainage lines, hand washing facilities, hose connections for clean up purposes, cardinal points of the compass, and the routes of edible and inedible products through the plant, properly drawn to scale, shall be submitted to the regional supervisor. The official plant shall include toilet and dressing rooms, office space for the inspector and grader, store rooms for supplies used in the operations under inspection or grading, feeding rooms, and all rooms, compartments or passageways where products or any ingredients to be used in the preparation of products under inspection service or grading service will be handled or kept, and may include other rooms or compartments located in the building or buildings comprising the official plant. If rooms or compartments shown on the drawings are not to be included as part of the official plant this should be clearly indicated thereon. Specifications covering the height of ceilings, types of principal pieces of equipment, character of floors, walls, and ceilings, lighting, ventilation, water supply, and drainage, and such other notations as may be required, shall accompany the drawings. Construction or remodeling of buildings, facilities, or premises should not be initiated without prior approval of the drawings. Upon approval of drawings and specifications the application for grading service or inspection service may be approved.

(3) *Final survey and plant approval.* Prior to the inauguration of the grading service, or inspection service, a final survey of the plant and premises shall be made by the regional supervisor or his assistant to determine if the plant is constructed and facilities are installed in accordance with the approved drawings and the regulations in this part. The plant may be approved only when these requirements have been met, except that conditional approval for a specified limited time may be granted only under emergency conditions of restricted availability of facilities and construction materials, provided practices suitable to the Administrator are employed to effect adequate sanitary conditions in the plant.

(f) *Rejection of application.* Any application for grading service or inspection service may be rejected by the Administrator (1) for noncompliance, by the applicant, with the act or the regulations in this part, or (2) whenever the product involved is owned by, or located on the premises of, a person currently denied the benefits of the act. Each such applicant shall be notified immediately of the reasons for the rejection.

(g) *Withdrawal of application.* Any application for grading or inspection service may be withdrawn by the applicant at any time before the service is performed upon payment by the applicant, of all expenses incurred by the Administration in connection with such application.

(h) *Order of service.* Grading service or inspection service shall be performed, insofar as practicable, in the order in which application therefor is made except that precedence may be given to any application for an appeal inspection or appeal grading.

§ 70.5 *Fraud or misrepresentation.* Any willful violation of the regulations in this part, the use of the terms "Government graded," "Federal-State graded," or terms of similar import in the labeling or advertising of any product without stating in conjunction therewith the U. S. grade of the product, or any willful misrepresentation or deceptive or fraudulent practice found to be made or committed by any person in connection with:

(a) The making or filing of an application for any grading service or inspection service;

(b) The use of any grading certificate or inspection certificate issued pursuant to the regulations in this part, or the use of any official identification;

(c) The use of the terms "United States" or "U. S." in conjunction with the grade of the product;

(d) The use of any of the aforesaid terms or an official identification in the labeling or advertising of any product; or

(e) The use, in connection with any product, of a facsimile form which simulates in whole or in part any official identification; may be deemed sufficient cause for debarring such person from any or all benefits of the act after opportunity for hearing has been accorded him; and, pending investigation and hearing the Administrator may, without hearing, direct that such person shall be denied the benefits of the act.

§ 70.6 *Political activity.* All graders and inspectors who are employees of the Department are forbidden during the period of their respective appointments, or licenses, to take an active part in political management or in political campaigns. Political activity in city, county, state, or national elections, whether primary or regular, or in behalf of any party or candidate, or any measure to be voted upon, is prohibited. This applies to all appointees, including, but not being limited to, temporary and cooperative employees and employees on leave of absence with or without pay. Willful violation of this section will constitute grounds for dismissal in the case of appointees and revocation of licenses in the case of licensees.

§ 70.7 *Interfering with a grader or inspector.* Any further benefits of the act and the regulations in this part may be denied any applicant who either personally or through an agent or representative interferes with or obstructs, by intimidation, threats, ridicule, or assault, or in any other manner, a grader or inspector in the performance of his duties.

§ 70.8 *Other applicable regulations.* Compliance with the regulations in this part shall not excuse failure to comply with any other Federal, or any State or municipal, applicable laws or regulations.

§ 70.9 *Publications.* Publications under the act and the regulations in this part shall be made in the FEDERAL REGISTER, the Service and Regulatory Announcements of the Department, and such other media as the Administrator may approve for the purpose.

§ 70.10 *Forms of certificates*—(a) *Grading certificates.* Grading certificates (including appeal grading certificates and regrading certificates) shall be issued on forms approved by the Administrator.

(b) *Inspection certificates.* Each inspection certificate issued pursuant to the regulations in this part shall be approved by the Administrator as to form, and:

(1) Each dressed poultry inspection certificate shall show the class or classes of poultry, the quantity of product contained in the respective lot, and all pertinent information concerning the condition and wholesomeness thereof;

(2) Each food product inspection certificate shall show the names of the edible products covered by such certificate, the quantity of each such product, such shipping marks as are necessary to identify such products, and all pertinent information concerning the condition and wholesomeness thereof;

(3) Each export certificate shall show the respective names of the exporter and the consignee, the destination, the shipping marks, the numbers of the export stamps attached to the edible products to be exported and covered by the certificate, and the names of such products and the total net weight thereof.

(c) *Advance information.* Upon the request of an applicant, all or part of the contents of any grading certificate or inspection certificate issued to such applicant may be telephoned or telegraphed to him, or to any person designated by him, at his expense.

§ 70.11 *Identifying and marking products*—(a) *Approval of official identification.* (1) Any label or packaging material which bears any official identification shall be used only in such manner as the Administrator may prescribe. No label or packaging material bearing official identification may be used unless finished copies or samples of such labels and packaging material have been approved by the Administrator. No label bearing the official identification shall be printed for use until the printer's final proof has been approved by the Administrator; and no label, other than labels for shipping containers or containers for institutional packs, bearing any official identification shall be used until finished copies or samples of such labels have been approved by the Administrator. Final approval may be given to printer's final proof or photostatic copies of labels for shipping containers or containers for institutional packs, and no such labels shall be used until such proofs or copies have been approved by the Administrator. A label which bears official identification shall not bear any statement that is false or misleading, and if labels in the name of the same packer or distributor, or bearing the same brand name, are used on the same or similar products which are prepared from products which are not inspected, the diameter of the inspection mark, or combination inspection and grading mark, used on labels for inspected products shall be equal to at least one-tenth of the length of the label, plus at least one-tenth of the width of the label. If the labeling is printed or otherwise applied directly on the container, the principal display panel of such container shall, for this purpose, be considered as the label.

(b) *Products that may be individually identified; information required on grade mark.* Only the following products may be individually identified with a grade mark if the respective product is of A Quality or B Quality: Dressed poultry, and ready-to-cook poultry. Except as otherwise authorized each grade mark which is to be used shall conspicuously indicate the U. S. grade of the product which it identifies, and shall indicate whether the bird is "young" or "mature" or "old," and shall include one of the following phrases: "Federal-State Graded," "Government Graded," or a phrase of similar import. Such grade mark shall be contained within the outline of a shield of such design as may be prescribed or approved by the Administrator.

(c) *Use of grade mark and inspection mark with respect to the same product.* The Administrator is authorized to prescribe and approve the form of the grade mark and inspection mark that may be used individually or in combination with respect to the same product.

(d) *Marking inspected products*—(1) *Wording and form of the inspection mark.* Except as otherwise authorized, the inspection mark permitted to be used with respect to inspected and certified edible products shall include wording as follows: "Inspected for wholesomeness by U. S. Department of Agriculture." This wording, in such form as the Administrator may prescribe or approve, shall be contained within a circle. The Administrator may approve the use of abbreviations of such inspection mark; and such approved abbreviations shall have the same force and effect as the inspection mark. The inspection mark or approved abbreviation thereof, as the case may be, may be applied to the inspected and certified edible product or to the packaging material of such product. The inspection mark, or the approved abbreviation thereof, shall, when used on packaging material, be printed on such material or on a label to be affixed to the packaging material, and the name of the packer or distributor of such product must be legibly printed on the packaging material or label, as the case may be, excepting that on shipping containers and containers for institutional packs the inspection mark may be stenciled on the container and when the inspection mark is so stenciled, the name and address of the packer or distributor may be applied by the use of a stencil or a rubber stamp.

(2) *Wording on labels.* Each trade label to be approved for use pursuant to this section with respect to any inspected and certified edible product shall bear the true name of the edible product, the name and address of the packer or distributor thereof, and, in prominent letters and figures of uniform size, the inspection mark, as aforesaid; and the label shall also bear, in such manner as may be prescribed or approved by the Administrator, the plant number, if any, of the official plant in which such product was inspected and certified.

(3) *Formulas required.* Copies of each trade label submitted for approval pursuant to this section shall, when the Administrator requires, be accompanied by a statement showing the kinds and percentages of the ingredients comprising the edible product with respect to which the label is to be used. Approximate percentages may be given in cases where the percentages of ingredients may vary from time to time, if the limits of variation are stated.

(4) *Wording permitted on food products containing poultry products.* Any trade label which is to be affixed to a container of any food product containing poultry product which is packed under the supervision of an inspector in any official plant may bear the phrase: "The poultry product contained herein has been inspected and certified at a plant where Federal inspection is maintained." Each such trade label shall also be subject to the applicable provisions of this section.

(5) *Labels in foreign languages.* Any trade label to be affixed to a container of any edible products for foreign commerce may be printed in a foreign language. However, the inspection mark shall appear on the label in English, but, in addition, may be literally translated into such foreign language. Each such trade label which is to be printed in a foreign language must be approved pursuant to this section.

(6) *Use of approved labels.* Trade labels approved for use pursuant to this section shall be used only for the purpose for which approved.

(e) *Marking dressed poultry which was certified as having been produced under sanitary requirements.* The Administrator is authorized to prescribe and approve the manner in which dressed poultry which was processed in accordance with minimum standards for sanitation, facilities, and operating procedures in official plants may be marked for identification purposes.

§ 70.12 *Supervision of marking and packaging*—(a) *Evidence of label approval.* No grader or inspector shall authorize the use of official identification for any graded or inspected product unless he has on file evidence that such official identification or packaging material bearing such official identification has been approved in accordance with the provisions of § 70.11.

(b) *Affixing of official identification.* (1) No official identification or any abbreviation, copy or representation thereof may be affixed to or placed on or caused to be affixed to or placed on any product or container thereof except by a grader or an inspector or under the supervision of a grader or an inspector or other person authorized by the Administrator. All such products shall have been inspected and certified or graded or both. The grader or inspector shall have su-

pervision over the use and handling of all material bearing any official identification.

(2) Each container of inspected and certified edible products to be shipped from one official plant to another official plant for further processing shall be marked for identification and shall show the following information:

(i) The name of the inspected and certified edible products in the container;

(ii) The name and address of the packer or distributor of such product;

(iii) The net weight of the container;

(iv) The inspection mark permitted to be used pursuant to the regulations in this part, unless the containers are sealed or otherwise identified in such manner as may be approved by the Administrator; and

(v) The plant number of the official plant where the products were packed.

(c) *Packaging.* No container which bears or may bear any official identification or any abbreviation or copy or representation thereof may be filled in whole or in part except with edible products which were inspected and certified or graded or both and are at the time of such filling, sound, wholesome and fit for human food. All such filling of containers shall be under the supervision of an inspector or grader.

§ 70.13 *Retention labels.* An inspector or grader may use such labels, devices and methods as may be approved by the Administrator for the identification (a) of products which are held for further examination, and (b) all equipment and utensils which are to be held for proper cleaning.

§ 70.14 *Prerequisites to grading and inspection.* Grading and inspection of products shall be rendered pursuant to the regulations in this part and under such conditions and in accordance with such methods as may be prescribed or approved by the Administrator.

§ 70.15 *Accessibility of products.* Each product for which grading service or inspection service is requested shall be so placed as to disclose fully its class, quality, quantity, and conditions as the circumstances may warrant.

§ 70.16 *Time of grading or inspection in an official plant.* The grader or inspector who is to perform the grading or inspection in an official plant shall be informed, in advance, of the hours when such grading or inspection will be required. Graders and inspectors shall have access at all times to every part of any official plant to which they are assigned.

§ 70.17 *Report of inspection work and grading work.* Reports of the work of inspection and grading carried on within official plants shall be forwarded to the Administrator by the inspector and grader in such manner as may be specified by the Administrator.

(a) *Information to be furnished to inspectors and graders.* When inspection service or grading service is performed within an official plant, the applicant for such inspection or grading shall furnish to the inspector or grader rendering such service such information as may be required for the purposes of this section.

(b) *Reports of violations.* Each inspector and each grader shall report, in the manner prescribed by the Administrator, all violations of and noncompliance with the act and the regulations in this part of which he has knowledge.

§ 70.18 *Fees and charges.*—(a) *Payment of fees and charges.* (1) Fees and charges for any grading or inspection shall be paid by the applicant for the service in accordance with the applicable provisions of this section and, if so required by the Administrator, such fees and charges shall be paid in advance.

(2) Fees and charges for any grading or inspection performed by any grader or inspector who is a salaried employee of the Department shall, unless otherwise required pursuant to subparagraph (3) of this paragraph, be paid by check, draft, or money order payable to the Treasurer of the United States and remitted promptly to the Administration.

(3) Fees and charges for any grading or inspection pursuant to a cooperative agreement with any State or person shall be paid in accordance with the terms of such cooperative agreement.

(b) *Grading service on a fee basis.* (1) Unless otherwise provided in this section, the fees to be charged and collected for any grading service (other than for an appeal grading) on a fee basis shall be based on the applicable rates specified in paragraph (d) of this section.

(2) In the event the aforesaid applicable rates specified in paragraph (d) of this section are deemed by the Administrator to be inadequate fully to reimburse the Administration for all costs and other items paid or incurred by the Administration in connection with such service, the fees for such service shall not be based on the rates specified in paragraph (d) of this section, but shall be based on the time required to perform such service and the travel of each grader at the rate of $3.00 per hour for the time actually required.

(3) If an applicant requests that any grading service be performed on a holiday or a non-work day, he may be charged for such service at a rate one and one-half times the rate which would be applicable for such service if performed on a day other than a holiday or a non-work day.

(c) *Fees for appeal grading.* The fees to be charged for any appeal grading shall be double the fee specified in the grading certificate from which the appeal is taken: *Provided,* That the fee for any appeal grading requested by the United States, or any agency or instrumentality thereof, shall be not more than that set forth in the grading certificate from which the appeal is taken. If the fee on the certificate from which the appeal is taken is based on a contract, then the fee for such appeal grading shall be double the amount specified in paragraph (d) of this section for the applicable volume of product appeal graded. If the result of any appeal grading discloses that a material error was made in the grading appealed from, no fee shall be required.

(d) *Poultry grading fees.* For each grading of any lot of poultry, whether live, dressed, or ready-to-cook, the following fees shall be applicable:

| | |
|---|---|
| For 500 pounds or less | $1.50 |
| For 501 to 1,500 pounds, inclusive | 2.25 |
| For 1,501 to 3,000 pounds, inclusive | 3.00 |
| For 3,001 to 6,000 pounds, inclusive | 4.00 |
| For 6,001 to 10,000 pounds, inclusive | 6.00 |
| For 10,001 to 20,000 pounds, inclusive | 10.00 |
| For each additional 10,000 pounds or fraction thereof, in excess of 20,000 pounds | 3.00 |

(e) *Inspection service on a fee basis.* Fees to be charged and collected for inspection services furnished on a fee basis shall be based on the time required to render such services including, but not being limited to, the time required for the travel of the inspector or inspectors in connection therewith, at the rate of $3.25 per hour for each inspector for the time actually required.

(f) *Fees for additional copies of grading certificates and inspection certificates.* Additional copies, other than those provided for in § 70.30 and § 70.35, of any grading certificates or inspection certificates may be supplied to any interested party upon payment of a fee of $1.00 for each set of five or fewer copies.

(g) *Traveling expenses and other charges.* Charges may be made to cover the cost of traveling and other expenses incurred by the Administration in connection with the performance of any grading service or inspection service.

(h) *Additional charges.* With respect to any grading service performed in a freight or express car or any other place where the entire lot of the product is not readily accessible to the grader, a charge of $5.00 shall be made in addition to the applicable rates specified in paragraph (d) of this section.

(i) *On a contract basis.* Fees to be charged and collected for any grading service or inspection service, other than for an appeal grading, on a contract basis shall be those provided for in such contract. The fees to be charged for any appeal grading shall be as provided in paragraph (c) of this section.

(j) *Fees for grading service or inspection service performed under cooperative agreement.* The fees to be charged and collected for any grading service or inspection service performed under cooperative agreement shall be those provided for by such agreement.

(k) *Disposition of fees for inspections made under cooperative agreement.* Fees for inspection under a cooperative agreement with any State or person shall be disposed of in accordance with the terms of such agreement. Such portion of the fees collected under a cooperative agreement as may be due the United States shall be remitted to the Administration.

INSPECTION

§ 70.19 *Manner of handling products in an official plant.* Unless otherwise specified in the regulations in this part or by the Administrator, products which are to be further processed under inspection in an official plant shall be prepared and handled in such official plant only in such manner as may be prescribed or approved by the Administrator and under the supervision of an inspector.

§ 70.20 *Ante-mortem inspection.* Ante-mortem examination of poultry may be required by the Administrator as a prerequisite to any inspection; and such ante-mortem examination shall be carried out under such conditions and in accordance with such methods as may be prescribed or approved by the Administrator.

§ 70.21 *Evisceration.* No viscera or any part thereof shall be removed from any dressed poultry which is to be processed under inspection in any official plant, except at the time of evisceration and inspection. Each carcass to be eviscerated shall be opened so as to expose the organs and the body cavity for proper examination by the inspector and shall be prepared immediately after inspection as eviscerated poultry. If a carcass is frozen, it shall be thoroughly thawed before being opened for examination by the inspector. Each carcass, or all parts comprising such carcass, shall be examined by the inspector: *Provided,* That the Administrator may, whenever he deems it advisable and under such conditions as he may prescribe, authorize the removal from such carcass or parts as aforesaid, of any part thereof prior to such inspection if such part will not be used in the preparation of any edible product.

§ 70.22 *Carcasses held for further examination.* Each carcass, including all parts thereof, in which there is any lesion of disease, or other condition, which might render such carcass or any part thereof unfit for human food, and with respect to which a final decision cannot be made on first examination by the inspector, shall be held for further examination. The identity of each such carcass, including all parts thereof, shall be maintained until a final examination has been completed.

§ 70.23 *Condemnation and treatment of carcasses.* Each carcass, or any part thereof, which is found to be unsound, unwholesome, or otherwise unfit for human food shall be condemned by the inspector and shall receive such treatment, under the supervision of the inspector as will prevent its use for human food and preclude dissemination of disease through consumption by animals.

§ 70.24 *Certification of carcasses.* Each carcass and all parts and organs thereof which are found by the inspector to be sound, wholesome, and fit for human food shall be certified as provided in this part.

§ 70.25 *Reinspection of edible products.* (a) Any inspected and certified edible product may be brought into an official plant only if the container of such product is marked for identification in the manner prescribed in § 70.12 (b) (2) and the product is reinspected by an inspector at the time it is brought into such plant. Upon reinspection, if any such product or portion thereof is found to be unsound, unwholesome, or otherwise unfit for human food, such product, or portion thereof, shall be condemned and shall receive such treatment as that provided in § 70.23.

(b) Any product which is prepared under inspection in an official plant shall be inspected in such plant as often as the inspector deems it necessary in order to ascertain whether such product is sound, wholesome, and fit for human food at the time such product leaves such plant. Upon any such inspection, if any such product or portion thereof is found to be unsound, unwholesome, or otherwise unfit for human food, such product or portion thereof shall be condemned and shall receive such treatment as that provided in § 70.23.

(c) All substances and ingredients used in the manufacture or preparation of any edible product shall be clean, sound, wholesome, and fit for human food.

§ 70.26 *Edible products for canning.* Only inspected and certified edible products may be canned in an official plant; and such edible products shall be processed and handled in compliance with the following requirements:

(a) Immediate containers (whether of metal, glass, or other material) shall be cleaned thoroughly by washing in an inverted position with running water of a temperature of at least 180° F. prior to filling with edible products; and precaution shall be taken to avoid any subsequent soiling of the inner surfaces of such containers.

(b) Only perfect closure is acceptable for hermetically sealed containers; and heat processing of the products in such containers shall follow immediately after closing.

(1) Except as provided in paragraph (c) of this section, such products shall be so processed at such temperature and for such period of time as will insure preservation of the products under usual conditions of storage and transportation.

(2) Immediately after closing, and again after the containers have cooled sufficiently for handling after heat processing, careful examination shall be made by competent plant employees of all containers to ascertain whether such containers are perfectly sealed. The edible products in such containers as are defectively closed or sealed shall, as promptly as practicable, be filled into other containers, hermetically sealed, and heat processed unless the containers are promptly placed in a cooler at a temperature not exceeding 36° F. under conditions that will promptly and effectively chill them. Such chilled containers of products shall be opened and the contents removed and reprocessed immediately after removal from the cooler: *Provided,* That if such containers remained in the cooler for a period of 24 hours or longer, the contents shall be inspected by an inspector prior to the reprocessing thereof. Failure to comply with the provisions of this paragraph shall subject the edible products to condemnation.

(c) After heat processing, and after the containers have cooled sufficiently for handling, the containers shall be examined by competent plant employees and shall not be passed unless showing the external characteristics of sound containers, that is, there is no bulging or slack or loose tin.

(d) After heat processing, any containers of edible products showing characteristics of short vacuum or overstuffed containers shall, when an inspector deems it necessary in order to determine whether spoilage of the product has taken place, be incubated under the supervision of an inspector, after which the containers shall be opened and sound products passed for food and spoiled products condemned.

(e) Edible products may, when authorized by the national supervisor, and under such conditions as he may prescribe or approve, be canned without steam-pressure cooking, and such products shall be labeled "Perishable, keep under refrigeration."

(f) Each lot of canned edible products shall be identified, during the handling preparatory to heat processing, by tagging the baskets, cases, or containers with a tag which will change color on going through the heat processing or by other effective means which will positively prevent failure to heat process.

(g) Facilities shall be provided to incubate at least representative samples of fully processed canned edible products. The incubation shall consist of holding the samples for at least 10 days at about 98° F. The extent to which incubation tests shall be required will depend on conditions such as the efficiency of the plant in conducting canning operations, the kind of equipment used, and the degree of efficiency at which such equipment is maintained.

(1) In the event the official plant fails to provide suitable facilities for incubation of test samples of any lot of fully processed canned edible products, the inspector in charge may require holding of the entire lot under such conditions and for such period of time as will, in his discretion, be necessary to ascertain the stability of the product.

(2) The inspector in charge may, prior to completion of any required incubation of a representative sample, permit lots of fully processed canned edible products to be shipped from the official plant when he has no reason to suspect unsoundness of such products; however, such shipments shall be made under circumstances which will assure the return of the products to the plant for reinspection should such action be indicated by the incubation results.

(h) All canned products, excepting those in glass, shall be plainly and permanently marked, by code or otherwise, on the containers, with the identity of the contents and date of canning. If the marking is by code, its meaning shall be on record in the office of the inspector in charge.

§ 70.27 *Products contaminated by polluted water; procedure for handling.* (a) In the event there is polluted water (including, but not being limited to, flood water and harbor water) in an official plant, all edible products that have been contaminated by the water shall be condemned.

(b) After the polluted water has receded, all walls, ceilings, posts, and floors of the rooms and compartments involved, including the equipment therein, shall, under the supervision of an inspector, be cleansed thoroughly. An adequate supply of hot water, under

pressure, is essential for effective cleansing. After cleansing, a solution of sodium hypochlorite containing approximately ½ of 1 percent of available chlorine (5,000 parts per million), or other disinfectant approved by the national supervisor, shall be applied; and all metal surfaces shall be rinsed thoroughly with water to prevent corrosion. Any such equipment that will afterwards be used in connection with any edible product shall be rinsed thoroughly with clean water before being used.

(c) Hermetically sealed containers of edible products which have been submerged in, or otherwise contaminated by, the polluted water shall be rehandled promptly under supervision of an inspector as follows:

(1) Such of the containers as are swollen or leaky or otherwise do not show the external characteristics of sound containers shall be segregated and the contents thereof condemned.

(2) Paper labels, if any, attached or affixed to the remaining containers shall be removed and the containers washed in warm soapy water; and, if necessary to remove rust and other foreign material, a brush shall be used.

(3) Thereafter, such containers shall be immersed in a solution of sodium hypochlorite containing not less than 100 parts per million of available chlorine, or other disinfectant approved specifically for this purpose by the national supervisor, and rinsed in clean fresh water and dried thoroughly. Any such containers which show extensive rusting or corrosion, such as might materially weaken the container, shall be opened under the supervision of an inspector. The edible products from such containers that are found by the inspector to be sound and wholesome shall be passed for human food.

(4) The remaining containers may be relacquered, if necessary, and then relabeled with approved labels applicable to the edible products therein.

(5) The identity of the canned edible products shall be maintained throughout all stages of the rehandling operation to insure correct labeling of the containers.

§ 70.28 *Preparation of animal food or similar uninspected articles in an official plant.* (a) When an article (including, but not being limited to, animal food) that will not be prepared for use as human food is prepared in any room or compartment in an official plant where edible products are prepared or handled (such room or compartments being herein referred to as "edible products department"), there shall be sufficient space allotted, and adequate equipment provided, so that the preparation of the article in no way interferes with the preparation or handling of the edible products. Where necessary, separate equipment shall be provided for the preparation of the article. To assure the maintenance of the requisite sanitary conditions in the edible products department, the operations incident to the preparation of the article shall be subject to the same sanitary requirements as apply to the edible products department. Preparation of the article shall be limited to those hours during which the official plant operates under the supervision of an inspector. The ingredients used in the preparation of the article shall, unless otherwise approved by the national supervisor, be such as may be used in the preparation of an edible product. The article may be stored in, and distributed from, the edible products department if the article is properly identified.

(b) When any article (including, but not being limited to, animal food) that will not be prepared for use as human food, is prepared in any part of an official plant other than an edible products department (such part of the plant being herein referred to as "inedible products department"), the area in which such article is prepared shall be distinctly separated from all edible products departments. Edible products and inedible products may be brought from any edible products department into any inedible products department, but no edible product or inedible product from an inedible products department may be brought into an edible products department except under such conditions as may be prescribed or approved by the national supervisor. Any such articles as are in sealed containers or are handled in the manner prescribed or approved by the national supervisor may be brought into an edible products department. Diseased carcasses or diseased parts of any carcass shall not be used in the preparation of any animal food. Trucks or containers used for the transportation of edible products or inedible products into an inedible products department shall be cleaned before being returned to or brought into an edible products department. Sufficient space shall be allotted and adequate equipment and facilities provided so that the preparation of the article does not interfere with the preparation of edible products in the plant or the maintenance of the requisite sanitary conditions in the official plant. The preparation of any article shall be subject to supervision by an inspector.

(c) The immediate container of any such article that is prepared in an official plant shall be conspicuously labeled so as to distinguish it from human food.

§ 70.29 *Appeal inspections; how made.* Any interested party may, if dissatisfied with any decision of an inspector relating to any inspection, file an appeal from such decision. Any such appeal from a decision of an inspector shall be made to his immediate superior having jurisdiction over the subject matter of the appeal. Review of such appeal findings, when requested, shall be made by the immediate superior of the employee of the Department making the appeal inspection.

§ 70.30 *Inspection certificates; issuance and disposition*—(a) *Issuance and disposition of dressed poultry inspection certificates.* (1) Upon the request of an interested party, any inspector is authorized to issue a dressed poultry inspection certificate with respect to any lot of dressed poultry inspected by him. Each certificate shall be signed by the inspector who made the inspection covered by the certificate, and if more than one inspector participated in the inspection of the lot of poultry, each such inspector shall sign the certificate with respect to such lot.

(2) The original of each inspection certificate, issued pursuant to this section, and not to exceed three copies thereof, shall, immediately upon issuance, be delivered or mailed to the applicant or person designated by him. One copy shall be filed in the office of the regional supervisor serving the area in which the inspection was performed, and the remaining copies to be disposed of in such manner as the Administrator may approve. Additional copies of any such certificate may be furnished to any interested party as provided in § 70.18 (f).

(b) *Food product inspection certificates; issuance and disposition.* (1) Upon the request of an interested party, any inspector is authorized to issue a food product inspection certificate with respect to any inspected and certified edible product after suitable examination of the product has been made by the inspector.

(2) The original of each food product inspection certificate, and not to exceed two copies thereof, if requested, shall, immediately upon issuance, be delivered or mailed to the applicant or person designated by him. Another copy shall be filed in the office of the regional supervisor serving the area in which such certificate was issued, and one copy shall be forwarded to the Administrator. The last named two copies shall be retained until otherwise ordered by the Administrator.

(c) *Export certificates; issuance and disposition.* (1) Upon the request of an exporter, any inspector is authorized to issue an export certificate with respect to the shipment to any foreign country of any inspected and certified edible product after suitable examination of the product has been made by the inspector.

(2) Each export certificate shall be issued in quintuplicate; the original shall be delivered to the exporter who requested such certificate; and the duplicate copy shall be delivered to the agent of the railroad or other carrier transporting such products from the United States. The triplicate copy of such export certificate shall be forwarded to the Administrator; the quadruplicate copy shall be filed in the office of the regional supervisor serving the area in which such export certificate was issued; and the memorandum copy shall be retained by the inspector for filing. The last named three copies shall be retained until otherwise ordered by the Administrator.

GRADING

§ 70.31 *General.* Grading service performed with respect to any quantity of product shall, as the case may require, be on the basis of an examination, pursuant to the regulations in this part, of each unit thereof or of each unit in the representative sample thereof drawn by a grader. Whenever the grading service is performed on a representative sample basis, such sample shall be drawn and

consist of not less than the minimum number of containers as indicated in the following table:

[Minimum number of containers comprising a representative sample]

| Containers in lot: | *Containers in sample* |
|---|---|
| 3 containers, or less | (1) |
| 4 to 10, inclusive | 3 |
| 11 to 20, inclusive | 4 |
| 21 to 50, inclusive | 7 |
| 51 to 100, inclusive | 10 |
| In excess of 100 containers | (2) |

[1] All containers.
[2] Ten percent of the number of containers in the lot.

§ 70.32 *Live poultry.* Grading service performed with respect to any quantity of live poultry shall, as the case may require, be on the basis of an examination, pursuant to regulations in this part, of each unit thereof or of each unit in the representative sample thereof drawn by a grader. Such poultry may be identified with official identification on a lot basis only.

§ 70.33 *Dressed poultry and ready-to-cook poultry*—(a) *In an official plant.* Grading service performed in an official plant with respect to dressed poultry or ready-to-cook poultry shall, as the case may require, be on the basis of each individual carcass or on a representative sample basis.

(1) Only such ready-to-cook poultry which has been inspected and certified, pursuant to the regulations in this part, or has been inspected and passed by any other official inspection system which is acceptable to the Administrator, may be graded.

(2) Only such dressed poultry or ready-to-cook poultry which has been graded, on an individual carcass basis, as A Quality or B Quality may be individually identified with the appropriate grade mark, and any container of such dressed poultry or ready-to-cook poultry may also be so identified. The grading of ready-to-cook poultry shall be performed prior to the disjointing or cutting up of the respective carcass.

(3) If the dressed poultry or ready-to-cook poultry is of C Quality only the bulk container of such dressed poultry or ready-to-cook poultry may be identified with the appropriate grade mark even though the grading may have been performed on an individual carcass basis.

(b) *At terminal markets and other receiving points.* Grading service performed with respect to dressed poultry or ready-to-cook poultry at terminal markets and other receiving points may be on a representative sample basis. Only such dressed poultry which was processed in an official plant and is graded on an individual carcass basis may be individually identified with a grade mark. Only ready-to-cook poultry which was inspected and certified and is marked with the inspection mark or in accordance with the provisions of § 70.12 (b) (2) may be graded.

§ 70.34 *Basis of acceptability of other official inspection systems*—(a) *General.* Any poultry inspection system may be deemed to be acceptable to the Administrator which (1) is conducted under the authority of laws, ordinances, or similar enactments of the State, county, city, or other political subdivision in which is located the official plant at which the ready-to-cook poultry is prepared and submitted for grading service; and (2) imposes at least the requirements set forth in paragraph (b) of this section: *Provided,* That no such inspection system shall be deemed acceptable to the Administrator with respect to any official plant in which ready-to-cook poultry is prepared if he finds at any time that such requirements are not adequately enforced.

(b) *Requirements as to manner of inspection.* (1) The inspection shall be made by a State, county or city inspector who is a qualified veterinarian or under the supervision of a qualified veterinarian. All such inspectors shall be employed by the State, county, city, or other political subdivision in which the official plant is located.

(2) The inspection shall include postmortem examination of each poultry carcass during the evisceration operation.

(3) All carcasses which show evidence of disease or any other condition which may render them unwholesome or unfit for food shall be condemned and shall be destroyed for food purposes under the supervision of an inspector. Each carcass and part thereof which has been inspected and passed or containers of carcasses or parts thereof shall bear the identifying inspection symbol of the other official inspection system and the marking devices or labels shall be in the custody of the inspector at all times.

(c) *Determining compliance with paragraph (b) of this section.* A qualified veterinary supervisor of the poultry grading service of the Administration shall investigate the manner of operation of the inspection system to determine the adequacy of the post-mortem examination and the compliance with the requirements contained in this section prior to approving the official plant for the grading of ready-to-cook poultry. This supervisor as well as any official graders who may be stationed in the official plant shall periodically observe the inspection operations in the official plant to determine whether the requirements of this section are being met. If at any time the inspector fails to enforce the requirements as set forth in the inspection system, grading service may be withdrawn from the official plant.

§ 70.35 *Certificates* — (a) *Issuance.* Each grader shall issue a grading certificate covering each product graded.

(b) *Disposition.* The original of each grading certificate, issued pursuant to this section, and not to exceed three of the copies thereof, shall, immediately upon issuance, be delivered or mailed to the applicant or person designated by him. One copy shall be filed in the office of grading which serves the area in which the grading service was performed, and the remaining copies shall be disposed of in such manner as the Administrator may approve. Additional copies of any such certificate may be furnished to any interested party as provided in § 70.18 (f).

§ 70.36 *Application for regrading of a graded product; regrading certificates*—(a) *Application for regrading of a graded product.* An application for a regrading of any previously graded product may be made at any time by any interested party, and such application shall clearly state the reasons for requesting the regrading. The provisions of the regulations relative to grading service shall apply to regrading service.

(b) *Regrading certificates.* Immediately after a regrading has been completed, a regrading certificate shall be issued showing the results of such regrading; and such certificate shall thereupon supersede, as of the time of issuance of the regrading certificate, the grading certificate previously issued for the product involved. Each regrading certificate shall clearly set forth the number and date of the grading certificate which it supersedes. The provisions of §§ 70.10 and 70.35 shall, whenever applicable, also apply to regrading certificates except that copies of such regrading certificates shall be furnished each interested party of record.

§ 70.37 *Appeal grading*—(a) *Application for appeal grading.* An application for an appeal grading may be made by any interested party who is dissatisfied with any determination stated in any grading or regrading certificate only if the indentity of the product, or representative sample thereof, on the basis of which a determination was made has not been lost, and such application for the appeal grading is made within two days following the day on which the grading was performed. Upon approval by the Administrator, the time within which an application for an appeal grading may be made may be extended.

(b) *How to obtain appeal grading.* Appeal grading may be obtained by filing a request therefor (1) with the Administrator, (2) with the grader who issued the grading certificate with respect to which the appeal grading is requested, (3) with the immediate superior of such grader, or (4) with the officer in charge of any office of grading. The application for appeal grading shall clearly state the reasons therefor and may be accompanied by a copy of the aforesaid grading certificate or any other information the applicant may have secured regarding the product, at the time of grading, from which the appeal is requested. Such application may be made orally (in person or by telephone), in writing, or by telegraph. If made orally, written confirmation may be required.

(c) *Record of filing time.* A record showing the date and hour when each such application for appeal grading is received shall be maintained in such manner as the Administrator may prescribe.

(d) *When an application for an appeal grading may be refused.* Notwithstanding the provisions of paragraph (a) of this section, if it appears to the Administrator that the reasons for an appeal grading are frivolous or not substantial, or that the quality or condition of the products has undergone a ma-

terial change since the grading from which the appeal is made, or the identical products that were examined to ascertain the grade thereof cannot be made accessible for reexamination, or the act or regulations in this part have not been complied with, the Administrator may refuse the applicant's request for the appeal grading; and such applicant shall be promptly notified of the reason for such refusal.

(e) *When an application for appeal grading may be withdrawn.* An application for appeal grading may be withdrawn by the applicant at any time before the appeal grading is made upon payment, by the applicant, of all expenses incurred by the Administration in connection with such application.

(f) *Who shall perform the appeal grading.* An appeal grading of any graded product shall be made by any grader (other than the one from whose grading the appeal is made) designated for this purpose by the Administrator; and, whenever practicable, such appeal grading shall be conducted jointly by two such graders.

(g) *Appeal grading by immediate superior.* Notwithstanding the provisions of this section, whenever the immediate superior of a grader has evidence that such grader incorrectly graded a product, such superior shall immediately make a regrading of the product.

(h) *Order of performance of appeal gradings.* Appeal gradings shall be performed, insofar as practicable, in the order in which applications therefor are received; and any such application may be given precedence pursuant to § 70.4.

(i) *Appeal grading certificates.* Immediately after an appeal grading has been completed, an appeal grading certificate shall be issued showing the results of such appeal grading. Such certificate shall thereupon supersede the grading certificate for the product involved and such supersedure shall be effective as of the time of issuance of the grading certificate with respect to which the appeal is made. Each appeal grading certificate shall clearly set forth the number and date of the grading certificate which it supersedes. The provisions of §§ 70.10 and 70.35 shall, whenever applicable, also apply to appeal grading certificates except that copies of such appeal grading certificates shall be furnished each interested party of record.

§ 70.38 *Superseded certificates.* Whenever any grading certificate is superseded in accordance with the regulations in this part such certificate shall become null and void as of the effective time of supersedure. If the original and all copies of such superseded certificate are not delivered to the person issuing the regrading certificate or appeal grading certificate, he shall notify such persons as he considers necessary to prevent fraudulent use of the superseded certificate.

SANITARY REQUIREMENTS

§ 70.39 *Minimum standards for sanitation, facilities, and operating procedures in official plants.* Except as otherwise provided herein the provisions of this section shall apply with respect to grading service and inspection service in all official plants other than with respect to the grading of live poultry. The table set forth in this section indicates some of the types of material which may be used in the construction of equipment, utensils and facilities for use in the plant.

BUILDING AND PLANT FACILITIES

(a) *Construction and repair of buildings.* The buildings shall be of sound construction and kept in good repair, and shall be of such construction as to prevent the entrance or harboring of rodents.

(1) *Outside openings.* (i) The doors, windows, skylights and other outside openings of the plant, except receiving rooms and feeding rooms shall be protected by properly fitted screens and other suitable devices, against the entrance of flies and other insects.

(ii) Outside doors, except in receiving rooms and feeding rooms shall be self-closing and so hung that not over ¼ inch clearance remains when closed. Screen doors shall open toward the outside of the building.

(b) *Rooms and compartments.* Rooms and compartments used for edible products shall be separate and distinct from inedible products departments and from rooms where live poultry is held or slaughtered. Separate rooms shall be provided when required for conducting processing operations in a sanitary manner; and all rooms shall be of sufficient size to permit the installation of the necessary equipment for processing operations and the conduct of such operations in a sanitary manner.

(1) *Separate rooms for various types of operations conducted.* The official plant should have separate rooms for each of the following operations depending upon the various types of operations conducted; but in no case shall the receiving or feeding of live poultry or killing operations be permitted in rooms in which eviscerating operations are performed:

(i) The receiving and feeding of live poultry.

(ii) Killing, scalding, and roughing operations.

(iii) Pinning, finishing, and chilling and packing operations for dressed poultry.

(iv) Evisceration operations. Final pinning of dressed poultry and chilling and packaging of edible products may be performed in this room. Openings in walls for conveyor lines are permissible.

(v) Inedible products departments.

(vi) Refuse room.

(2) *Rooms and compartments for inspection of carcasses, or parts thereof.* Rooms and compartments in which carcasses or parts thereof are held for further inspection shall be in such numbers and such locations as the needs of the inspection in the plant may require. These rooms and compartments shall be equipped with locks and keys and the keys shall not leave the custody of the inspector in charge of the plant. All such rooms and compartments shall be marked conspicuously with the word "retained" in letters not less than 2 inches high.

(3) *Coolers and freezers.* Coolers and freezers of adequate size and capacity shall be provided to reduce the internal temperature of dressed poultry and ready-to-cook poultry prepared and otherwise handled in the plant to 36° F. within 24 hours unless other cooling facilities are available.

(4) *Refuse rooms.* Refuse rooms shall be entirely separate from other rooms in the plant, shall have tight fitting doors and be properly ventilated.

(5) *Storage and supply rooms.* The storage and supply rooms shall be in good repair, kept dry, and maintained in a sanitary condition.

(6) *Boiler room.* The boiler room shall be a separate room, if necessary, to prevent its being a source of dirt and objectionable odors entering any room where dressed poultry or edible products are prepared, processed, handled, and stored.

(7) *Inspector's office.* Furnished office space, including but not being limited to light, heat, and janitor service shall be provided rent free in the official plant, for the exclusive use for official purposes of the inspector or grader and the Administration. The room or rooms set apart for this purpose must meet with the approval of the regional supervisor and be conveniently located, properly ventilated and provided with lockers or cabinets suitable for the protection and storage of supplies and with facilities suitable or inspectors and graders to change clothing.

(8) *Toilet rooms.* No toilet rooms shall open directly into any room where poultry products are exposed and each such room shall be provided with self-closing doors.

(c) *The floors, walls, ceiling, partitions, posts, doors, and other parts of all compartments shall be of such material, construction, and finish as will make them susceptible of being readily and thoroughly cleaned*—(1) *Floors.* (i) All floors, except those in receiving rooms and feeding rooms and floors which are kept dry, shall be constructed of hardened concrete, or of tile laid closely together with impervious joint material, or of other similar impervious material and kept in good repair.

(ii) The floors in killing, ice-cooling, ice-packing and eviscerating rooms shall be graded to permit run-off with no standing water and in new construction and renovated plants the pitch shall be not less than ¼ inch per foot to drains.

(2) *Ceilings and walls.* (i) Ceilings and walls in rooms and compartments where exposed edible products are processed, handled or stored shall have tiled, enameled, or other smooth surface impervious to moisture.

(ii) Cooler and freezer rooms shall have interior surfaces impervious to moisture so as to permit thorough cleaning.

(3) *Blood disposal.* (i) Adequate facilities shall be provided for the disposal of blood in a sanitary manner.

(ii) When bleeding troughs are used they shall be long enough to catch the blood during the bleeding process and shall be cleaned daily. Such troughs shall be installed so as to pitch at least ½ inch per foot toward a smooth metal

catch basin or basins, of sufficient capacity for a day's operation at peak production, or shall be flushed continuously.

(d) *There shall be an efficient drainage and plumbing system for the plant and premises*—(1) *Drains and gutters.* All drains and gutters shall be properly installed with approved traps and vents. The drainage and plumbing system must permit the quick run-off of all water from plant buildings, and surface water around the plant and on the premises; and all such water shall be disposed of in such a manner as to prevent a nuisance or health hazard.

(2) *Sewerage and plant wastes.* (i) The sewerage system shall have adequate slope and capacity to remove readily all waste from the various processing operations and to minimize, and if possible to prevent stoppage and surcharging of the system.

(ii) Catch basins which are connected with the sewerage system shall be suitably located but not near any edible products department or in any area where products are unloaded from, or loaded into, vehicles. To facilitate cleaning such basins shall have inclined bottoms and be provided with suitable covers.

(iii) Toilet soil lines shall be separate from house drainage lines to a point outside the buildings; and drainage from toilet bowls and urinals shall not be discharged into a grease catch basin.

(iv) All floor drains shall be equipped with traps, constructed so as to minimize clogging; and the plumbing shall be installed so as to prevent sewage from backing up and from flooding the floor.

(v) Floor drainage lines should be of metal and at least 4 inches in diameter and open into main drains of at least 8 inches in diameter and shall be properly vented to the outside air.

(vi) Where refrigerators are equipped with drains, such drains should be properly trapped and should discharge through an air gap into the sewer system. All new installations, and all replacements, of refrigerators equipped with drains shall meet these requirements.

(e) *The water supply shall be ample, clean, and potable with adequate facilities for its distribution in the plant, and its protection against contamination and pollution.* (1) Hot water at a temperature not less than 180° F. shall be available for sanitation purposes.

(2) Hose connections with steam and water mixing valves or hot water hose connections shall be provided at convenient locations throughout the plant for cleaning purposes.

(3) The refuse rooms shall be provided with a hot water supply and adequate facilities for washing refuse cans and other equipment in the rooms; and the rooms, cans, and equipment shall be cleaned after each day's use.

(f) *Modern lavatory accommodations, and properly located facilities for cleaning utensils and hands shall be provided.* (1) Adequate lavatory and toilet accommodations, including, but not being limited to, running hot water and cold water, soap, and towels, shall be provided. Such accommodations shall be in or near toilet and locker rooms and also at such other places in the plant as may be essential to the cleanliness of all personnel handling products.

(2) Sufficient metal containers shall be provided for used towels and other wastes.

(3) The water supply in all hand washing facilities shall be operated by foot pedal or knee control or shall be of a continuous-flow type.

(4) Durable signs shall be posted conspicuously in each toilet room and locker room directing employees to wash their hands before returning to work.

(5) Toilet facilities shall be provided according to the following formula.

| Persons of same sex: | *Toilet bowls required* |
|---|---|
| 1 to 15, inclusive | 1 |
| 16 to 35, inclusive | 2 |
| 36 to 55, inclusive | [1] 3 |
| 56 to 80, inclusive | [1] 4 |
| For each additional 30 persons in excess of 80 | [1] 1 |

[1] Urinals may be substituted for toilet bowls but only to the extent of ⅓ of the total number of bowls stated.

(g) *Lighting and ventilation.* There shall be ample light, either natural or artificial or both, of good quality and well distributed, and sufficient ventilation for all rooms and compartments to insure sanitary conditions.

(1) All rooms in which poultry is killed, eviscerated, or otherwise processed shall have at least 10 foot candles of light intensity on all working surfaces except that at the grading and inspection stations such light intensity shall be of 50 foot candles. In all other rooms there shall be provided at least 4 foot candles of light intensity when measured at a distance of 30 inches from the floor.

(2) All rooms shall be adequately ventilated to eliminate objectionable odors and minimize moisture condensation.

EQUIPMENT AND UTENSILS

(h) *Equipment and utensils used for the preparation, processing, or otherwise handling any product in the plant shall be suitable for the purpose intended and shall be of such material and construction as will facilitate their thorough cleaning and insure cleanliness in the preparation and handling of products*—(1) *Material.* Insofar as it is practical, equipment and utensils shall be made of metal or other impervious material. Trucks and receptacles used for handling inedible products shall be of similar construction and shall be conspicuously and distinctly marked and shall not be used for handling any edible products.

(2) *Batteries.* Batteries should be constructed entirely of metal and have metal dropping pans so as to permit proper and complete washing and cleaning. Batteries that are not made entirely of metal shall be replaced with metal batteries whenever replacement becomes necessary.

(3) *Metal refuse containers.* Metal refuse containers with covers shall be provided; and such containers shall be kept covered.

(4) *Scalding equipment.* (i) Scalding equipment, tank or spray type, shall be made of metal and have smooth surfaces, and be of such construction as to permit proper and complete washing and cleaning.

(ii) The scalding tanks, when used, shall be so constructed (including, but not being limited to, the use of a back flow preventer) as to permit water to enter continuously at the rate of ¼ gallon per bird per minute and to flow out through an overflow near the top.

(iii) The overflow outlets in scalding equipment shall be of sufficient size to permit feathers and water to be carried off.

(iv) The overflow, draw-off valves, and sediment basin drain shall discharge into a floor or valley drain.

(5) *Mechanical pickers.* When necessary, safety guards shall be installed around moving machine parts of mechanical pickers, and such guards shall be of such construction as not to be difficult or laborious to remove or to keep clean. Sheet metal or metal grills fastened down with sufficient bolts and wing nuts are preferable.

(6) *Wax finishing.* When wax dipping is used, metal troughs shall be provided to catch the wax removed from the dipped poultry. Acceptable facilities and methods shall be employed in reclaiming the wax.

(7) *Ice chilling vats.* (i) Chilling vats or tanks used for chilling dressed poultry should be, and all replacements thereof and all chilling vats or tanks used for chilling ready-to-cook poultry shall be, made of metal or other hard-surfaced impervious material.

(ii) Ice shovels shall be smooth surfaced and made of metal.

(8) *Grading and packing bins.* Where grading bins are used for dressed poultry, they shall be of sufficient number and capacity to handle the grading adequately without the use of makeshift bins; and all dressed poultry shall be kept off the floor. Grading bins may be made of metal or enameled wood and shall be constructed and maintained in such a manner as to allow easy and thorough cleaning. All replacements of such bins shall, however, be of metal.

(9) All equipment and utensils used in the killing, roughing, pinning, chilling and packing rooms shall be of metal or other impervious material and constructed so as to permit proper and complete cleaning.

(10) *Conveyors.* (i) Conveyors used in the preparation of ready-to-cook poultry shall be of metal and of such construction as to permit thorough and ready cleaning and easy identification of viscera with its carcass and so designed as will present each carcass or all parts thereof in a way that will permit adequate and efficient inspection.

(ii) Overhead conveyors shall be so constructed and maintained that they will not allow grease, oil, or dirt to accumulate on the drop chain or shackle which shall be of non-corrosive metal.

(iii) Non-metallic belt-type conveyors used in moving edible products shall be of water-proof composition.

(iv) When individual trays or other acceptable equipment are not used during eviscerating operations, each carcass shall be suspended and a metal

trough shall be provided beneath the conveyor to extend from the point where the carcass is opened to the point where the viscera has been completely removed, and such troughs shall be flushed continuously by a water spray.

(11) Inspection, eviscerating, and cutting tables shall be made of metal and have coved corners and be so constructed and placed to permit thorough cleaning.

(12) In plants where no conveyors are used, each carcass shall be eviscerated in an individual metal tray of seamless construction.

(13) Water spray washing equipment with sufficient water pressure to thoroughly and efficiently wash carcasses shall be used for washing carcasses inside and out.

(14) Watertight metal receptacles shall be used for entrails and other waste resulting from preparation of eviscerated poultry.

(15) Watertight trucks and receptacles for holding or handling diseased carcasses and diseased parts of carcasses shall be so constructed as to be readily and thoroughly cleaned; such trucks and receptacles shall be marked in a conspicuous manner with the word "condemned" in letters not less than 2 inches high and, when required by the inspector in charge, shall be equipped with facilities for locking and sealing.

(16) Freezing rooms shall be adequately equipped to freeze ready-to-cook poultry solid in less than 60 hours. Freezing rooms shall be equipped with floor racks or pallets and fans to insure air circulation.

(17) Cooling racks should be made of metal and be readily accessible for thorough washing and cleaning. All replacements of cooling racks shall be made of metal.

(18) Trucks and receptacles in which carcasses or parts thereof are held for further inspection shall be in such numbers and in such locations as the needs of the inspection in the plant may require. They shall be equipped for locking by means of lock and key and the key shall not leave the custody of the inspector in charge of the plant. Such trucks and receptacles shall be marked conspicuously with the word "retained" in letters not less than 2 inches high.

(i) *All equipment shall be so placed as to be readily accessible for all processing and cleaning operations*—(1) *Mechanical pickers.* When used in the plant, mechanical pickers shall be so installed as to be accessible for thorough cleaning and removal of the accumulation of feathers.

(j) *Equipment and utensils used in official plant.* Equipment and utensils used in the official plant shall not be used outside the official plant except under such conditions as may be prescribed or approved by the national supervisor, and equipment used in the preparation of any article (including, but not being limited to animal, food), from inedible material shall not be used outside of the inedible products department except under such conditions as may be prescribed or approved by the national supervisor.

MAINTENANCE OF SANITARY CONDITIONS AND PRECAUTIONS AGAINST CONTAMINATION OF PRODUCTS

(k) *The premises shall be kept free from refuse, waste materials, and all other sources of objectionable odors.*

(l) *Rooms, compartments, or other parts of the official plant in which products are handled and kept shall be kept clean and in sanitary condition.* (1) All feathers, blood, offal, birds or parts of birds too severely damaged to be salvaged, and all discarded containers and other materials shall be completely disposed of daily.

(2) All windows, doors, and light fixtures in the official plant shall be kept clean.

(3) All docks and rooms shall be kept clean and free from debris and unused equipment and utensils.

(4) Live poultry receiving docks and receiving rooms shall be of such construction as readily to permit their thorough cleaning.

(5) Floors in feeding rooms shall be thoroughly cleaned and with such regularity as may be necessary to maintain them in a sanitary condition.

(6) The killing, roughing, and pinning room shall be kept clean and free from offensive odors at all times.

(7) The walls, floors, and all equipment and utensils used in the killing, roughing and pinning room shall be thoroughly cleaned after each day's operation.

(8) The floors in the killing, roughing, and pinning room shall be cleaned frequently during roughing and finishing operations and be kept reasonably free from accumulated blood, feathers, manure, water, and dirt.

(9) All equipment in the toilet room and locker room, as well as the room itself, shall be kept clean, sanitary, and in good repair.

(10) Cooler and freezer rooms shall be free from objectionable odors of any kind and shall be maintained in a sanitary condition (including, but not being limited to, the prevention of drippings from refrigerating coils onto products).

(m) *Equipment and utensils used for preparing or otherwise handling any product shall be kept clean and in a sanitary condition and in good repair.* (1) Batteries and dropping pans shall be cleaned regularly and the manure removed from the plant daily.

(2) The feed mixer shall be cleaned daily.

(3) Scalding tanks shall be completely emptied and thoroughly cleaned as often as may be necessary but not less frequently than once a day.

(4) Ice shovels shall be kept clean, free of corrosion, and shall be stored off the floor.

(5) All equipment and utensils used in the killing, roughing, and pinning rooms shall be thoroughly washed and cleaned after each day's operation. The chilling and packing room and equipment and utensils used therein shall be maintained in a clean and sanitary condition.

(6) Graders' and packers' gloves and grading bins shall be washed daily and used only for grading or packing, as the case may be.

(7) Chilling vats or tanks, if practicable, shall be emptied after each use. They shall be thoroughly cleaned once daily, and after each cleaning operation they shall be sanitized with such compounds or by such methods as may be approved or prescribed by the Administrator.

(8) Thawing: When frozen or chilled poultry is to be eviscerated, adequate tanks or vats shall be provided with running tap water or air-circulated water for thawing such poultry. Such poultry shall not be thawed in still water and the water used for thawing shall be changed after each lot of poultry is thawed. If water is heated it shall not be heated above 70° F. The tanks or vats shall be equipped with properly installed overflow pipes to discharge the water over floor drains or a valley drain. Where mechanical devices are not used for removing thawed carcasses from the tanks or vats, the tanks or vats, as the case may be, shall be of such size as to enable employees to remove poultry without getting inside the tanks or vats.

(9) When synchronized overhead conveyors and tray conveyors are used, the trays shall be completely washed and sanitized after being automatically emptied of inedible viscera.

(10) When a conveyor tray operation is used, such trays shall be of metal of seamless construction and shall be completely washed and sanitized after each use.

(11) Tables, shelves, bins, trays, pans, knives, and all other tools and equipment used in the preparation of eviscerated or ready-to-cook poultry shall be kept clean and sanitary at all times. Cleaned equipment and utensils shall be drained on racks and shall not be nested.

(12) Drums, cans, tanks, vats, and other receptacles used to hold or transport dressed poultry, or eviscerated poultry, shall be kept in a clean and sanitary condition.

(n) *Operations and procedures involving the preparation, storing, or handling of any product shall be strictly in accord with clean and sanitary methods.* (1) There shall be no handling or storing of materials which create an objectionable condition in rooms, compartments, or other places in the plant where any product is prepared, stored, or otherwise handled.

(2) The pinning and finishing operations shall be performed in a part of the room that is away from the killing and roughing operations.

(3) Blood from the killing operation shall be confined to a relatively small area and kept from being splashed about the room.

(4) In finishing and cleaning dressed poultry, feed shall be removed from the crop and the fecal material in the cloaca shall be removed by venting and such operations shall be completed prior to the final washing, chilling, and packaging of dressed poultry.

(5) The head of each dressed poultry carcass shall be washed thoroughly to

remove feed from the mouth and blood from the head and mouth.

(6) In the final washing, the carcass shall be passed through a system of sprays providing an abundant supply of fresh clean water either under pressure or scrubbing action.

(7) Grading and packaging: Dressed poultry may be graded and packaged in the killing, roughing, pinning, chilling, and packing room; however, such poultry shall be graded and packed in an area of the room which is well isolated from the killing and roughing operation.

(8) The floors in the eviscerating room shall be kept clean and reasonably dry during eviscerating operations and free of all refuse.

(9) Conveyors shall be operated at such speeds as will permit a sanitary eviscerating operation and will permit adequate inspection for condition and wholesomeness.

(10) Mechanized packaging equipment shall be maintained in good sanitary condition.

(11) All offal resulting from the eviscerating operation shall be removed as often as necessary to prevent the development of a nuisance.

(12) Paper and other material used for lining barrels or other containers in which products are packaged shall be of such kinds as do not tear readily during use, but remain intact when moistened by the product.

(13) Protective coverings shall be used for the product, as it is distributed from the plant, as will afford adequate protection for the product against contamination by any foreign substance (including, but not being limited to, dust, dirt, and insects), considering the means intended to be employed in transporting the product from the plant.

(14) Refuse may be moved directly to loading docks only for prompt removal.

(15) Cleanliness and hygiene of personnel: (i) All employees coming in contact with exposed edible products or edible products handling equipment shall wear clean garments and shall keep their hands clean at all times while thus engaged.

(ii) Hands of employees handling dressed poultry or edible products or edible products handling equipment shall be free of infected cuts, boils, and open sores at all times while thus engaged.

(iii) Every person after each use of toilet or change of garments shall wash his hands thoroughly before returning to duties that require the handling of dressed poultry or edible products, or containers therefor, or edible products handling equipment.

(iv) Neither smoking nor chewing of tobacco shall be permitted in any room where exposed edible products are prepared, processed, or otherwise handled.

(o) *Temperatures and procedures necessary for cooling and freezing of poultry.* Temperatures and procedures which are necessary for cooling and freezing of poultry in accordance with sound commercial practice shall be maintained in the coolers and freezers, and ice chilling temperatures and procedures shall also be in accordance with sound commercial practice.

(1) *Ice chilling.* (i) Only ice manufactured or produced from potable water may be used for ice chilling. The ice shall be handled and stored in a sanitary manner. If of block-type, the ice shall be washed by spraying with clean water before crushing. Metal ice crushers shall be washed at least once daily.

(ii) Enough clean crushed ice shall be used to maintain a temperature in vats or tanks under 40° F. at all times during chilling. Any dressed poultry carcass weighing less than 8 pounds shall not be permitted to remain in a chilling vat or tank for longer than six hours unless the water is drained. Any dressed poultry carcass weighing 8 pounds or more shall not be permitted to remain in a chilling vat or tank for longer than eight hours unless the water is drained. Any such poultry carcass, however, shall not be allowed to remain in a chilling vat or tank after the internal temperature of the carcass has been lowered to 36° F. unless the water is drained.

(2) *Air chilling.* In air chilling, dressed poultry shall be passed through a spray of clean water immediately following the removal of the feathers, and then hung on racks. Thereupon the racks of dressed poultry shall be placed in a refrigerated room with moderate air movements and a temperature which will reduce the internal temperature of the carcass to from 36° F. to 40° F., both inclusive, within 24 hours.

(3) *Freezing.* (i) When dressed poultry is packaged in bulk or shipping containers, the carcasses should be individually wrapped or packaged in water-vapor resistant cartons or the containers should be lined with heavy water-vapor resistant paper so as to assure adequate overlapping of the lining to completely surround the carcasses and to permit unsealed closure or sealing in such a manner that water-vapor loss from the product is considerably retarded or prevented. The dressed poultry should receive an initial rapid freezing under such packaging, temperature, air circulation, and stacking conditions which will result in freezing the carcasses solid in less than 60 hours. Any carcass weighing less than 8 pounds should freeze solid in from 30 to 40 hours, whereas a carcass weighing more than 8 pounds should freeze solid in from 48 to 60 hours. (The approximate highest temperatures which will attain this result under average to most favorable conditions, are −10° F. with circulated air and −20° F. with still air; however, freezing temperatures of −20° F. to −40° F. are desirable.)

(ii) Frozen dressed poultry should be stored at 0° F. or below, with temperatures maintained as constant as possible.

(4) Immediately after packaging, all dressed poultry and ready-to-cook poultry, other than that which is ice-packed or shipped from the plant in a refrigerated carrier, should be moved into the freezer; except, that a period not exceeding 72 hours shall be permitted for transportation and temporary holding before placing in the freezer provided such poultry is held at not above 36° F. The provisions in subparagraphs (1) and (3) of this paragraph, shall be applicable to ready-to-cook poultry.

(5) When poultry is packed in ice in barrels or other containers the barrels and containers shall be covered and shall have an adequate number of drain holes to permit water to drain out.

(p) *Precaution against flies, rats, mice, and other vermin.* Every practicable precaution shall be taken to exclude flies, rats, mice, and other vermin from the official plant.

(q) *Persons affected with communicable disease.* No person affected with any communicable disease (including, but not being limited to, tuberculosis) in a transmissible stage shall be permitted in any room or compartment where exposed or unpacked dressed poultry or edible products are prepared, processed, or otherwise handled.

(r) *Table showing types of materials.*

| Equipment, utensils, and facilities | Iron | Rubber | Concrete | Stainless steel and monel metal | Aluminum | Galvanized iron | Copper (tin plated) | Porcelain or glazed tile |
|---|---|---|---|---|---|---|---|---|
| Batteries | --- | --- | --- | A | A | A | --- | --- |
| Overhead conveyors | A | --- | --- | A | --- | A | --- | --- |
| Conveyor track | A | --- | --- | A | --- | A | --- | --- |
| Shackle chain | --- | --- | --- | A | --- | A | --- | --- |
| Shackles | --- | --- | --- | A | --- | A | --- | --- |
| Blood trough | A | --- | A | A | A | A | --- | --- |
| Scalding vat | A | --- | --- | A | --- | A | --- | --- |
| Mechanical pickers | A | A | --- | A | A | A | --- | --- |
| Mechanical scrubber | A | A | --- | A | A | A | --- | --- |
| Wax dipping tank | A | --- | --- | A | A | A | --- | --- |
| Trough for catching wax | A | --- | --- | A | A | A | --- | --- |
| Water-spray cooling chamber | --- | --- | --- | A | A | A | --- | --- |
| Opening trough | --- | --- | --- | A | A | A | --- | --- |
| Eviscerating pans | --- | --- | --- | A | A | A | --- | --- |
| Inspection table (those parts which come in contact with product) | --- | --- | --- | A | A | A | --- | --- |
| Eviscerating trough | --- | --- | --- | A | A | A | --- | --- |
| Framework (of equipment) | A | --- | --- | A | --- | A | --- | --- |
| Inside and outside washer | --- | A | --- | A | A | A | --- | A |
| Gizzard, heart, and liver trimming tables | --- | --- | --- | A | A | --- | --- | --- |
| Defrosting trucks | --- | --- | --- | A | A | A | --- | --- |
| Defrosting tanks | --- | --- | A | A | --- | A | --- | A |
| Cooling racks | --- | --- | --- | A | A | A | --- | --- |
| Tanks or vats and other equipment used for cooling products | --- | --- | A | A | A | A | --- | --- |
| Above-the-floor grease traps | --- | --- | --- | A | A | A | --- | --- |
| Utensils for handling edible products | --- | --- | --- | A | A | A | --- | --- |
| Boning and cooling tables, cutting surfaces | --- | --- | --- | A | A | A | --- | --- |
| Cooking kettles | A | --- | --- | A | A | A | A | --- |

§ 70.40 *Authority of Administrator to amend minimum standards for sanitation, facilities, and operating procedures in official plants.* The Administrator is authorized to amend the provisions in § 70.39; and such amended provisions shall be applicable to official plants.

SUBPART B—UNITED STATES SPECIFICATIONS FOR CLASSES, STANDARDS, AND GRADES OF POULTRY AND EDIBLE PRODUCTS THEREOF

§ 70.101 *United States specifications for kinds and classes of live poultry, dressed poultry, and ready-to-cook poultry.* The specifications contained in this section apply to live poultry, dressed poultry, and individual carcasses of ready-to-cook poultry in determining the kind of poultry and its class. The kinds of poultry are as follows: Chickens, turkeys, ducks, geese, guineas, and pigeons.

(a) *Chickens.* For the purpose of this section, the following classes of chickens are specified:

(1) *Broiler or fryer.* A broiler or fryer is a young chicken (usually under 16 weeks of age), of either sex, that is tender-meated with soft, pliable, smooth-textured skin and flexible breastbone cartilage.

(2) *Roaster.* A roaster is a young chicken (usually under 8 months of age), of either sex, that is tender-meated with soft, pliable, smooth-textured skin and breastbone cartilage that is somewhat less flexible than that of a broiler or fryer.

(3) *Capon.* A capon is an unsexed male chicken (usually under 10 months of age) that is tender-meated with soft, pliable, smooth-textured skin.

(4) *Stag.* A stag is a male chicken (usually under 10 months of age) with coarse skin, somewhat toughened and darkened flesh, and considerable hardening of the breastbone cartilage. Stags show a condition of fleshing and a degree of maturity intermediate between that of a roaster and a cock or old rooster.

(5) *Hen or stewing chicken or fowl.* A hen or stewing chicken or fowl is a mature female chicken (usually more than 10 months old) with meat less tender than that of a roaster, and non-flexible breastbone.

(6) *Cock or old rooster.* A cock or old rooster is a mature male chicken with coarse skin, toughened and darkened meat, and hardened breastbone.

(b) *Turkeys.* For the purpose of this section, the following classes of turkeys are specified:

(1) *Fryer.* A fryer is a young turkey (usually under 14 weeks of age), of either sex, that is tender-meated with soft, pliable, smooth-textured skin, and flexible breastbone cartilage.

(2) *Young hen turkey.* A young hen turkey is a young female turkey (usually under 8 months of age) that is tender-meated with soft, pliable, smooth-textured skin, and breastbone cartilage that is somewhat less flexible than in a turkey fryer.

(3) *Young tom turkey.* A young tom turkey is a young male turkey (usually under 8 months of age) that is tender-meated with soft, pliable, smooth-textured skin and breastbone cartilage that is somewhat less flexible than in a turkey fryer.

(4) *Mature hen turkey or old hen turkey.* A mature hen turkey or old hen turkey is a mature female turkey (usually over 10 months of age) with toughened flesh and hardened breastbone that may have coarse or dry skin and patchy areas of surface fat.

(5) *Mature tom turkey or old tom turkey.* A mature tom turkey or old tom turkey is a mature male turkey (usually over 10 months of age) with coarse skin, toughened flesh, and hardened breastbone.

(c) *Ducks.* For the purpose of this section the following classes of ducks are specified:

(1) *Broiler duckling or fryer duckling.* A broiler duckling or fryer duckling is a young duck (usually under 8 weeks of age) of either sex, that is tender-meated and has a soft bill and soft windpipe.

(2) *Roasting duckling.* A young roasting duckling is a young duck (usually under 16 weeks of age), of either sex, that is tender-meated and has a bill that is not completely hardened and a windpipe that is easily dented.

(3) *Mature duck or old duck.* A mature duck or an old duck is a duck (usually over 6 months of age), of either sex, with toughened flesh, hardened bill, and hardened windpipe.

(d) *Geese.* For the purpose of this section, the following classes of geese are specified:

(1) *Young goose.* A young goose may be of either sex, is tender-meated, and has a windpipe that is easily dented.

(2) *Mature goose or old goose.* A mature goose or old goose may be of either sex and has toughened flesh and hardened windpipe.

(e) *Guineas.* For the purpose of this section, the following classes of guineas are specified:

(1) *Young guinea.* A young guinea may be of either sex and is tender-meated.

(2) *Mature guinea or old guinea.* A mature guinea or an old guinea may be of either sex and has toughened flesh.

(f) *Pigeons.* For the purpose of this section, the following classes of pigeons are specified:

(1) *Squab.* A squab is a young, immature pigeon of either sex, and is extra tender-meated.

(2) *Pigeon.* A pigeon is a mature pigeon of either sex, with coarse skin and toughened flesh.

§ 70.102 *United States specifications for standards of quality for live poultry on an individual bird basis*—(a) *General.* (1) The United States specifications for standards of quality for individual live birds contained in this section are applicable only to poultry of the kinds and classes set forth in § 70.101.

(2) Birds showing evidence of any disease or other condition which may render then unwholesome or unfit for human food shall not be included in any of the quality designations specified in this section.

(3) The following factors are considered in ascertaining the quality of an individual bird: (i) Health and vigor; (ii) feathering; (iii) conformation; (iv) fleshing; (v) fat covering; and (vi) the degree of freedom from defects.

(b) *Standards of quality*—(1) *A Quality or No. 1 Quality.* To be of A Quality or No. 1 Quality the live bird:

(i) Is alert, has bright eyes, and is of good health and vigor.

(ii) Is well feathered, with feathers showing luster or sheen and quite thoroughly covering all parts of the body; however, there may be a slight scattering of pinfeathers.

(iii) Is of normal physical conformation except that it may have a slightly curved breastbone or other slight abnormality in the shape of the breastbone which does not interfere with the normal distribution of the flesh. The bird may also have a slightly curved back. There may be a dent in the breastbone which does not exceed ⅛ inch in depth except that for turkeys the depth does not exceed ¼ inch.

(iv) Has a well developed, moderately broad and long breast that is well-fleshed throughout its entire length; and the thighs and back are well covered with flesh according to the age and sex of the bird.

(v) Has the breast, back, hips, and pin bones well covered with fat, except that a fryer (whether chicken or turkey) and a young tom turkey may have only a moderate amount of fat covering these parts, and a hen, stewing chicken, or fowl does not have excessive abdominal fat.

(vi) Is free from tears and broken bones; however, it may have slight scratches, slight skin bruises, and slight callouses (i. e., slightly thickened, hardened, and darkened areas of skin over the breastbone), if these conditions do not materially affect the appearance of the bird, especially the breast. It may also have slightly scaly shanks.

(2) *B Quality or No. 2 Quality.* To be of B Quality or No. 2 Quality the live bird:

(i) Is of good health and vigor.

(ii) Is fairly well feathered (i. e., some feathers may be lacking on some parts of the body); however, there may be a moderate number of pinfeathers.

(iii) Is of normal physical conformation except that it may have a slightly crooked breastbone which does not seriously interfere with the normal distribution of the flesh. It may also have a moderately crooked back and slightly misshapen legs and wings.

(iv) Is fairly well fleshed in relation to length and depth of body, with all parts fairly well covered with flesh according to the age and sex of the bird.

(v) Has sufficient coverage of fat on breast and legs to prevent a distinct appearance of the flesh through the skin; however, a hen, stewing chicken, or fowl may have excessive abdominal fat.

(vi) Is free from tears, broken bones, severe breast blisters, heavy callouses (i. e., thickened, hardened, and darkened areas of skin over the breastbone) and seriously scaly shanks; however, it may have moderate skin bruises and slight flesh bruises.

(3) *C Quality or No. 3 Quality.* A live bird that does not meet the requirements of B Quality or No. 2 Quality may be of C Quality or No. 3 Quality and such bird may:

(i) Be lacking in vigor.

(ii) Have a large number of pinfeathers over all parts of its body and complete lack of plumage feathers on the back.

(iii) Have definite deformities (including, but not being limited to, a crooked breastbone, hunchback, and slight crippling).

(iv) Have a poorly developed, narrow breast and thin covering of flesh over all parts of its body.

(v) Have only a small amount of fat in the feather tracts and is completely lacking in fat on back and thighs; and

(vi) Have skin bruises, small or moderate flesh bruises, and severe breast blisters; however, it has no broken bones.

The term "Reject" is not a standard of quality within the purview of this section; however, such term may be used

with respect to an individual live bird to indicate that it is affected by, or shows evidence of, any disease or condition (including, but not being limited to, large flesh bruises, severe discolorations, severe injury, and emaciation) which may render the bird unfit for human food.

§ 70.103 *United States specifications for standards of grades for live poultry*—(a) *General.* (1) The United States specifications for standards of grades for live poultry contained in this section are applicable to live poultry of the kinds and classes set forth in § 70.101 and are based upon United States specifications for standards of quality as set forth in § 70.102.

(2) Birds showing evidence of any disease or other condition which may render them unwholesome or unfit for human food shall not be included in any of the grade designations specified in this section.

(3) All terms in the United States specifications for standards of quality, as set forth in § 70.102, shall, when used in this section, have the same meaning as when used in the specifications.

(b) *Specifications for grades*—(1) *U. S. Grade A or U. S. No. 1.* Any lot of live poultry may be designated as U. S. Grade A or U. S. No. 1 if at least 90 percent, by count, of the birds are of A Quality or No. 1 Quality and the remainder are of B Quality or No. 2 Quality. When more than one container comprises the lot, no container shall have more birds of B Quality or No. 2 Quality than that specified in the following table:

[When lot consists of more than 1 container]

| Grade | Number of birds in container | Maximum number of B quality or No. 2 quality birds |
|---|---|---|
| U. S. Grade A or U. S. No. 1. | Less than 10 | 1 bird. |
| | 10 to 15, inclusive | 2 birds. |
| | 16 to 20, inclusive | 3 birds. |
| | 21 to 25, inclusive | 4 birds. |
| | 26 or more | 5 birds. |

(2) *U. S. Grade B or U. S. No. 2.* Any lot of live poultry may be designated as U. S. Grade B or U. S. No. 2 if at least 90 percent, by count, of the birds are of B Quality or No. 2 Quality, or better, and the remainder are of C Quality, or No. 3 Quality. When more than one container comprises the lot, no container shall have more birds of C Quality or No. 3 Quality than that specified in the following table:

[When lot consists of more than 1 container]

| Grade | Number of birds in container | Maximum number of quality or No. 3 quality birds |
|---|---|---|
| U. S. Grade B or U. S. No. 2. | Less than 10 | 1 bird. |
| | 10 to 15, inclusive | 2 birds. |
| | 16 to 20, inclusive | 3 birds. |
| | 21 to 25, inclusive | 4 birds. |
| | 26 or more | 5 birds. |

(3) *U. S. Grade C or U. S. No. 3.* Any lot of live poultry may be designated as U. S. Grade C or U. S. No. 3 if it consists of birds of not less than C quality or No. 3 Quality.

The term "No Grade" is not a grade within the meaning of this section. Such term may be applied to any lot of live poultry if such lot contains any birds of less than C Quality or No. 3 Quality or has not been graded in accordance with this section.

§ 70.104 *United States specifications for standards of quality for individual carcasses of dressed poultry and ready-to-cook poultry*—(a) *General.* (1) The United States specifications for standards of quality contained in this section are applicable to individual carcasses of dressed poultry and ready-to-cook poultry of the kinds and classes set forth in § 70.101.

(2) Carcasses found to be unsound, unwholesome, or unfit for food shall not be included in any of the quality designations specified in this section. If the carcass is dressed poultry, determination of unsoundness or unwholesomeness will be based on external characteristics only.

(3) The quality designations specified in this section may not be made applicable to dressed poultry that is not free from the following conditions: Dirty head; bloody head; dirty carcass; bloody carcass; dirty vent; dirty feet; fan feathers on the wing tips; garter feathers around the hock joints; neck feathers; and, if the crop is not removed, feed in the crop.

(4) The A Quality designation may not be made applicable to any poultry carcass if the poultry was wet picked in such a manner that the skin has been damaged by extended immersion in, or high temperature of, the water which resulted in immediate discoloration or may result in later objectionable discoloration.

(5) The following factors are considered in ascertaining, pursuant to this section, the quality of an individual carcass: (i) Conformation; (ii) fleshing; (iii) fat covering; (iv) the degree of freedom from pinfeathers and vestigial feathers (i. e., hair or down, as the case may be); (v) the degree of freedom from tears, cuts (including, but not being limited to, any cut for the removal of the crop), disjointed bones, and broken bones; (vi) the degree of freedom from discolorations of the skin and of the flesh and of blemishes and bruises of the skin and flesh; and (vii) the degree of freedom from freezer burn.

(6) In addition to the respective requirements specified in this section for A Quality, B Quality, and C Quality, the intensity, aggregate area involved, and locations of all (i) discolorations (whether or not caused by dressing operations), (ii) bruises, (iii) pinfeathers, and (iv) freezer burn, as such combination of defects detracts from the general appearance of the carcass, will also be considered in determining the particular quality of an individual carcass.

(b) *Standards of quality*—(1) *A Quality.* To be of A Quality the carcass:

(i) Is of normal physical conformation except that it may have a slightly curved breastbone or other slight abnormality in the shape of the breastbone which does not interfere with the normal distribution of the flesh. The carcass may also have a very slightly curved back. There may be a dent in the breastbone which does not exceed ⅛ inch in depth except that for turkeys the depth does not exceed ¼ inch.

(ii) Has a well-developed, moderately broad and long breast, well-fleshed throughout its entire length, with the flesh carrying sufficiently well up to the crest of the breastbone so that the breastbone is not prominent; and, with respect to young tom turkeys, there may be a slight thickening and slight pouchiness of the skin on the forepart of the breast. The legs are well covered with flesh.

(iii) Has the breast, back, hips, and pin bones well covered with fat except that chicken broilers or fryers, turkey fryers, and young tom turkers may have only a moderate amount of fat covering these parts, but a hen, stewing chicken, or fowl does not have excessive abdominal fat.

(iv) Is practically free from pinfeathers, especially on the breast, and is free from vestigial feathers (i. e., hair or down, as the case may be) if the carcass is dressed poultry. If the carcass is ready-to-cook poultry, it is free from protruding pinfeathers, practically free from nonprotruding pinfeathers, especially on the breast, and free from vestigial feathers.

(v) Is free from skin tears and cuts on the breast and legs; however, elsewhere on the carcass there may be tears and cuts (exclusive of the cuts usually made to remove the neck and viscera in the production of eviscerated poultry) the aggregate length of which does not exceed 1½ inches except that, with respect to any turkey carcass or goose carcass, such aggregate length does not exceed 3 inches. There are no sewn tears or cuts. The carcass has no disjointed bones or broken bones except that it may have one disjointed bone in either a leg or wing but only if there is no evidence of a related bruise or blood clot; and, if the carcass is of a chicken broiler or fryer, it may have one nonprotruding broken bone in a wing in addition to such disjointed bone but only if there is no evidence of a related bruise or blood clot. The wing tips may have been removed.

(vi) Is free from bruises and discolorations of the flesh on the breast and legs; however, elsewhere on the carcass there may be bruises and discolorations of the flesh showing not more than a slightly reddened color the aggregate area of which does not exceed the area of a circle ½ inch in diameter, except that, with respect to any turkey or goose carcass, such aggregate area does not exceed the area of a circle 1 inch in diameter. The carcass is free from skin bruises, on the breast and legs, the aggregate area of which exceeds the area of a circle ½ inch in diameter, and from skin bruises, elsewhere on the carcass, the aggregate area of which exceeds the area of a circle ¾ inch in diameter. With respect to any turkey or goose carcass, such aggregate area on the breast and legs does not exceed the area of a circle ¾ inch in diameter; and elsewhere on the carcass such aggregate area does not exceed the area of a circle 1½ inches in diameter. Notwithstanding the foregoing, the total aggregate area, on the breast and legs, of all such

flesh bruises, skin bruises, and all other discolorations and blemishes of the skin, is not in excess of the area of a circle 1 inch in diameter; and elsewhere on the carcass such total aggregate area is not in excess of the area of a circle 1½ inches in diameter. Furthermore, with respect to any turkey or goose carcass, such total aggregate area on the breast and legs is not in excess of the area of a circle 2 inches in diameter; and elsewhere on the carcass such total aggregate area is not in excess of the area of a circle 3 inches in diameter. The skin may show only slight reddening in the feather follicles on the neck, near the head, and on the wings because of improper bleeding.

(vii) Shows only slight freezer burn, or evidence thereof (i. e., a few pockmarks, or evidence thereof, none of which exceeds the area of a circle ⅛ inch in diameter).

(2) *B Quality.* To be of B Quality the carcass:

(i) Is of at least practically normal physical conformation except that it may have a dented, curved, and slightly crooked breastbone which does not seriously interfere with the normal distribution of the flesh. The carcass may also have a moderately crooked back or misshapen legs or misshapen wings.

(ii) Is sufficiently well-fleshed on the breast and legs so as to prevent a thin appearance and a prominent breastbone; however, a young tom turkey may have a pouchy, thick, and somewhat flabby skin on the forepart of the breast.

(iii) Has a sufficient coverage of fat on the breast and legs to prevent a distinct appearance of the flesh through the skin.

(iv) Has not more than a slight scattering of pinfeathers over the entire carcass with only relatively few on the breast and is free from vestigial feathers (i. e., hair or down, as the case may be) if the carcass is dressed poultry. If the carcass is ready-to-cook poultry, it is free from protruding pinfeathers and vestigial feathers but may have not more than a few scattered, nonprotruding pinfeathers.

(v) Is free from tears and cuts, on the breast and legs, the aggregate length of which exceeds 1½ inches; however, elsewhere on the carcass there may be tears and cuts (exclusive of the cuts usually made to remove the neck and viscera in the production of eviscerated poultry), the aggregate length of which does not exceed 3 inches except that, with respect to any turkey or goose carcass, such aggregate lengths do not exceed 3 inches on the breast and legs and 6 inches elsewhere on the carcass. There are no sewn tears or cuts. The carcass may have not more than a total of 2 disjointed bones in either the legs or wings, or both, but only if there is no evidence of a related bruise or blood clot, and, in addition, 1 broken bone in a leg or wing, but only if it is nonprotruding and does not show an excessive related bruise or blood clot. The wing tips may have been removed.

(vi) Is free from bruises and discolorations, of the flesh on the breast and legs, showing not more than a slightly darkened color and which in the aggregate is in excess of the area of a circle ½ inch in diameter; however, elsewhere on the carcass there may be bruises and discolorations of the flesh the aggregate area of which does not exceed the area of a circle 1½ inches in diameter, except that, with respect to any turkey or goose carcass, such aggregate area on the breast and legs does not exceed the area of a circle 1 inch in diameter, and, elsewhere on the carcass, it does not exceed the area of a circle 3 inches in diameter. The carcass is free from skin bruises, on the breast and legs, the aggregate area of which exceeds the area of a circle ¾ inch in diameter, and from skin bruises, elsewhere on the carcass, the aggregate area of which exceeds the area of a circle 1½ inches in diameter. With respect to any turkey or goose carcass, such aggregate area on the breast and legs does not exceed the area of a circle 1½ inches in diameter, and, elsewhere on the carcass, such aggregate area does not exceed the area of a circle 3 inches in diameter. Notwithstanding the foregoing, the total aggregate area on the breast and legs of all such flesh bruises, skin bruises, and all other discolorations and blemishes of the skin is not in excess of the area of a circle 1½ inches in diameter; and elsewhere on the carcass such total aggregate area is not in excess of the area of a circle 3 inches in diameter. Furthermore, with respect to any turkey or goose carcass, such total aggregate area on the breast and legs is not in excess of the area of a circle 3 inches in diameter; and elsewhere on the carcass such total aggregate area is not in excess of the area of a circle 6 inches in diameter. The skin may show not more than moderate reddening in the feather follicles on the neck, near the head, and on the wings and thighs because of improper bleeding.

(vii) Shows no more than moderate freezer burn, or evidence thereof, on any part of the carcass and no dried area in excess of the area of a circle ½ inch in diameter.

(3) *C Quality.* A carcass that does not meet the requirements of B Quality may be of C Quality and such carcass may:

(i) Be of abnormal physical conformation (i. e., possess serious abnormal physical conditions, including, but not being limited to, a crooked back and crooked breastbone) if it is fairly well fleshed.

(ii) Be poorly fleshed and a young tom turkey may have a thick, coarse skin and extended breast that is pouchy or flabby.

(iii) Be lacking in fat covering, over all parts of the carcass.

(iv) Have numerous pinfeathers and vestigial feathers (i e., hair or down, as the case may be) scattered over the entire carcass if the carcass is dressed poultry; if ready-to-cook poultry, the carcass is free from protruding pinfeathers and vestigial feathers, but may have nonprotruding pinfeathers that do not seriously detract from the appearance of the carcass.

(v) Have torn skin, disjointed bones, and broken bones but only if there is no evidence of a related severe bruise or blood clot. There are no sewn tears or cuts. Wing tips may have been removed.

(vi) Have numerous and large discolored areas or blemishes of the skin which may be accompanied by some reddening and darkening of the flesh beneath, if such discolored areas and blemishes do not render any part of the carcass unfit for food.

(vii) Show more than moderate freezer burn or evidence thereof (including, but not being limited to, numerous pockmarks or large dried areas) on any part of the carcass.

§ 70.105 *United States specifications for standards of grades for dressed poultry and ready-to-cook poultry*—(a) *General.* (1) The United States specifications for standards of grades for dressed poultry and ready-to-cook poultry are applicable to dressed poultry and ready-to-cook poultry of the kinds and classes as set forth in § 70.101 when individual carcasses are not separately identified and are based upon the United States specifications for standards of quality set forth in § 70.104 except the provisions in subparagraph (3) of this paragraph.

(2) When any lot of dressed poultry is graded on the basis of an examination of each carcass in a representative sample thereof, any carcass that would be of A Quality if it did not possess any of the following conditions shall, for the purpose of this section, be considered as being of B Quality; dirty or bloody head or carcass, dirty feet or vent, fan feathers or neck feathers or garter feathers, or feed in the crop. Any carcass that would be of B Quality or C Quality if it did not possess any of the foregoing conditions shall, for the purpose of this section, be considered as being of C Quality.

(3) All terms in the United States specifications for standards for quality set forth in § 70.104 shall, when used in this section, have the same meaning as when used in the specifications.

(4) The suggested weight specifications for dressed poultry and ready-to-cook poultry contained in paragraph (c) of this section are not incorporated in the standards of grades for dressed poultry and ready-to-cook poultry since weight, as such, is not a factor of grade for the purpose of the standards in this section. It is recommended, however, that each container of dressed poultry and ready-to-cook poultry contain carcasses of the weights specified in paragraph (c) of this section.

(b) *Specifications for grades*—(1) *U. S. Grade A.* Any lot of dressed poultry or ready-to-cook poultry composed of one or more containers of carcasses of the same kind and class may be designated as U. S. Grade A if not less than 90 percent, by count, of the carcasses in such lot are of A Quality, the remainder is of B Quality, and no individual container in such lot contains more carcasses of B Quality than in the proportion of 2 to each 12 carcasses in the container.

(2) *U. S. Grade B.* Any lot of dressed poultry or ready-to-cook poultry composed of one or more containers of carcasses of the same kind and class may be designated as U. S. Grade B if not less than 90 percent, by count, of the car-

casses in such lot are of at least B Quality, the remainder is of C Quality, and no individual container in such lot contains more carcasses of C Quality than in the proportion of 2 to each 12 carcasses in the container.

(3) *U. S. Grade C.* Any lot of dressed poultry or ready-to-cook poultry may be designated as U. S. Grade C if it consists of carcasses of not less than C Quality.

(c) *Suggested weight specifications for dressed poultry and ready-to-cook poultry.* The suggested weight specifications for dressed poultry and ready-to-cook poultry are contained in Tables I, II, III, and IV in this paragraph.

DRESSED POULTRY

TABLE I—CHICKENS

| Class of chickens | Weight range per carcass | | Weight range per dozen carcasses | |
|---|---|---|---|---|
| | Minimum | Maximum | Minimum | Maximum |
| Broilers or fryers | None | 1 pound 8 ounces | None | 18 pounds. |
| | Over 1 pound 8 ounces | 2 pounds | Over 18 pounds | 24 pounds. |
| | Over 2 pounds | 2 pounds 8 ounces | Over 24 pounds | 30 pounds. |
| | Over 2 pounds 8 ounces | 3 pounds | Over 30 pounds | 36 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces | Over 36 pounds | 42 pounds. |
| | Over 3 pounds 8 ounces | 4 pounds | Over 42 pounds | 48 pounds. |
| Roasters | Over 3 pounds | 3 pounds 8 ounces | Over 36 pounds | 42 pounds. |
| | Over 3 pounds 8 ounces | 4 pounds | Over 42 pounds | 48 pounds. |
| | Over 4 pounds | 4 pounds 8 ounces | Over 48 pounds | 54 pounds. |
| | Over 4 pounds 8 ounces | 5 pounds | Over 54 pounds | 60 pounds. |
| | Over 5 pounds | 5 pounds 8 ounces | Over 60 pounds | 66 pounds. |
| | Over 5 pounds 8 ounces | None | Over 66 pounds | None. |
| Capons | None | 6 pounds | None | 72 pounds. |
| | Over 6 pounds | 7 pounds | Over 72 pounds | 84 pounds. |
| | Over 7 pounds | 8 pounds | Over 84 pounds | 96 pounds. |
| | Over 8 pounds | 9 pounds | Over 96 pounds | 108 pounds. |
| | Over 9 pounds | 10 pounds | Over 108 pounds | 120 pounds. |
| | Over 10 pounds | None | Over 120 pounds | None. |
| Stags | None | 3 pounds | None | 36 pounds. |
| | Over 3 pounds | 4 pounds | Over 36 pounds | 48 pounds. |
| | Over 4 pounds | 5 pounds | Over 48 pounds | 60 pounds. |
| | Over 5 pounds | 6 pounds | Over 60 pounds | 72 pounds. |
| | Over 6 pounds | None | Over 72 pounds | None. |
| Cocks | None | 4 pounds | None | 48 pounds. |
| | Over 4 pounds | 5 pounds | Over 48 pounds | 60 pounds. |
| | Over 5 pounds | 6 pounds | Over 60 pounds | 72 pounds. |
| | Over 6 pounds | None | Over 72 pounds | None. |
| Hens or stewing chickens or fowl | None | 3 pounds | None | 36 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces | Over 36 pounds | 42 pounds. |
| | Over 3 pounds 8 ounces | 4 pounds | Over 42 pounds | 48 pounds. |
| | Over 4 pounds | 4 pounds 8 ounces | Over 48 pounds | 54 pounds. |
| | Over 4 pounds 8 ounces | 5 pounds | Over 54 pounds | 60 pounds. |
| | Over 5 pounds | None | Over 60 pounds | None. |

TABLE II—TURKEYS

| Class | Weight range per carcass | |
|---|---|---|
| | Mimimum | Maximum |
| Turkey fryers | None | 6 pounds. |
| | Over 6 pounds | 8 pounds. |
| | Over 8 pounds | 10 pounds. |
| Young hen turkeys or young tom turkeys | None | 6 pounds. |
| | Over 6 pounds | 8 pounds. |
| | Over 8 pounds | 10 pounds. |
| | Over 10 pounds | 12 pounds. |
| | Over 12 pounds | 14 pounds. |
| | Over 14 pounds | 16 pounds. |
| | Over 16 pounds | 18 pounds. |
| | Over 18 pounds | 20 pounds. |
| | Over 20 pounds | 22 pounds. |
| | Over 22 pounds | 24 pounds. |
| | Over 24 pounds | None. |
| Mature or old hen turkeys and mature or old tom turkeys. | None | 10 pounds. |
| | Over 10 pounds | 15 pounds. |
| | Over 15 pounds | 20 pounds. |
| | Over 20 pounds | None. |

DRESSED POULTRY—Continued

TABLE III—DUCKS, GEESE, GUINEAS, SQUABS, AND PIGEONS

| Kind and class | Weight range per carcass | | Weight range per dozen carcasses | |
|---|---|---|---|---|
| | Minimum | Maximum | Minimum | Maximum |
| Ducks (all classes) | None | 4 pounds | None | 48 pounds. |
| | Over 4 pounds | 5 pounds | Over 48 pounds | 60 pounds. |
| | Over 5 pounds | None | Over 60 pounds | None. |
| Geese (all classes) | None | 8 pounds | None | 96 pounds. |
| | Over 8 pounds | 10 pounds | Over 96 pounds | 120 pounds. |
| | Over 10 pounds | None | Over 120 pounds | None. |
| Guineas (all classes) | None | 1 pound 8 ounces | None | 18 pounds. |
| | Over 1 pound 8 ounces | 2 pounds 4 ounces | Over 18 pounds | 27 pounds. |
| | Over 2 pounds 4 ounces | None | Over 27 pounds | None. |
| Squabs and pigeons | None | 8 ounces | None | 6 pounds. |
| | Over 8 ounces | 11 ounces | Over 6 pounds | 8 pounds 6 ounces. |
| | Over 11 ounces | 14 ounces | Over 8 pounds 6 ounces | 10 pounds 8 ounces. |
| | Over 14 ounces | None | Over 10 pounds 8 ounces | None. |

TABLE IV—READY-TO-COOK POULTRY

| Kinds and classes | Weight range per carcass | |
|---|---|---|
| | Minimum | Maximum |
| Broilers or fryers | None | 1 pound 8 ounces. |
| | Over 1 pound 8 ounces | 2 pounds. |
| | Over 2 pounds | 2 pounds 8 ounces. |
| | Over 2 pounds 8 ounces | 3 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces. |
| Roasters | Over 2 pounds 8 ounces | 3 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces. |
| | Over 3 pounds 8 ounces | 4 pounds. |
| | Over 4 pounds | 4 pounds 8 ounces. |
| | Over 4 pounds 8 ounces | 5 pounds. |
| | Over 5 pounds | None. |
| Hens or stewing chickens or fowl | None | 2 pounds. |
| | Over 2 pounds | 2 pounds 8 ounces. |
| | Over 2 pounds 8 ounces | 3 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces. |
| | Over 3 pounds 8 ounces | 4 pounds. |
| | Over 4 pounds | 4 pounds 8 ounces. |
| | Over 4 pounds 8 ounces | 5 pounds. |
| | Over 5 pounds | 5 pounds 8 ounces. |
| | Over 5 pounds 8 ounces | None. |
| Cocks or old roosters | None | 2 pounds 8 ounces. |
| | Over 2 pounds 8 ounces | 3 pounds 8 ounces. |
| | Over 3 pounds 8 ounces | 4 pounds 8 ounces. |
| | Over 4 pounds 8 ounces | 5 pounds 8 ounces. |
| | Over 5 pounds 8 ounces | None. |
| Turkeys and geese (all classes) | None | 4 pounds. |
| | Over 4 pounds | 6 pounds. |
| | Over 6 pounds | 8 pounds. |
| | Over 8 pounds | 10 pounds. |
| | Over 10 pounds | 12 pounds. |
| | Over 12 pounds | 14 pounds. |
| | Over 14 pounds | 16 pounds. |
| | Over 16 pounds | 18 pounds. |
| | Over 18 pounds | 20 pounds. |
| | Over 20 pounds | None. |
| Ducks (all classes) | None | 3 pounds. |
| | Over 3 pounds | 3 pounds 8 ounces. |
| | Over 3 pounds 8 ounces | 4 pounds. |
| | Over 4 pounds | None. |
| Guineas (all classes) | None | 12 ounces. |
| | Over 12 ounces | 1 pound. |
| | Over 1 pound | 1 pound 4 ounces. |
| | Over 1 pound 4 ounces | 1 pound 8 ounces. |
| | Over 1 pound 8 ounces | None. |
| Pigeons (all classes) | None | 6 ounces. |
| | Over 6 ounces | 10 ounces. |
| | Over 10 ounces | 14 ounces. |
| | Over 14 ounces | None. |

(Pub. Law 759, 81st Cong., approved Sept. 6, 1950)

Issued at Washington, D. C., this seventh day of March 1951.

[SEAL] K. T. HUTCHINSON,
*Acting Secretary of Agriculture.*

[F. R. Doc. 51-3197; Filed, Mar. 12, 1951; 8:46 a. m.]

## CIVIL AERONAUTICS BOARD

### [ 14 CFR, Parts 20, 21, 22, 24, 25, 26, 27, 33, 34, 35, and 51 ]

AIRMAN IDENTIFICATION CARD

NOTICE OF PROPOSED RULE MAKING

Pursuant to authority delegated by the Civil Aeronautics Board to the Bureau of Safety Regulation, notice is hereby given that the Bureau will propose to the Board amendments of Parts 20, 21, 22, 24, 25, 26, 27, 33, 34, 35, and 51 of the Civil Air Regulations in substance as hereinafter set forth.

Interested persons may participate in the making of the proposed rules by submitting such written data, views, or arguments as they may desire. Communications should be submitted in duplicate to the Civil Aeronautics Board, attention Bureau of Safety Regulation, Washington 25, D. C. All communications received by April 13, 1951, will be considered by the Board before taking further action on the proposed rules. Copies of such communications will be available after April 17, 1951, for examination by interested persons at the Docket Section of the Board, Room 5412, Commerce Building, Washington, D. C.

No provisions of our currently effective Civil Air Regulations require the possession of positive identification data by certificated airmen while exercising the privileges of their airman certificates. The proposed amendments will make provision for such identification and will require that each certificated airman, after September 1, 1951, have in his possession an airman identification card (Form ACA 2135), which the Administrator would be authorized to issue subsequent to April 15, 1951.

This airman identification card shall contain, among other data, the airman's signature, picture, and one fingerprint. It is contemplated that each certificated airman shall complete an application for identification card (Form ACA 2134) and shall furnish documentary evidence of his personal identification, citizenship, place and date of birth, and the type of airman certificate held. It should be noted that an expired airman identification card (Form ACA 935) issued during World War II may serve as sufficient evidence in these matters. An applicant who has once possessed this expired identification card but is unable to produce it at the time of application may substitute a letter from the Airman Records Branch, Civil Aeronautics Administration, Washington 25, D. C., which, in effect, attests to the issuance and contents of the expired card.

It is proposed to amend Parts 20, 21, 22, 24, 25, 26, 27, 33, 34, 35, and 51 of the Civil Air Regulations by adding new §§ 20.58, 21.45, 22.32 (g), 24.47, 25.86, 26.37, 27.23, 33.46, 34.20, 35.21, and 51.6, each to read as follows:

*Identification.* After September 1, 1951, the holder of a certificate issued under the provisions of this part shall not exercise the privileges conferred by the certificate unless he has in his possession a current airman identification card which duly describes him. This identification card may be obtained from the Administrator who shall prescribe its form and the manner of applying for it.

These amendments are proposed under the authority of Title VI of the Civil Aeronautics Act of 1938, as amended. The proposed amendments may be changed in view of comments received in response to this notice of proposed rule making.

(Sec. 205 (a), 52 Stat. 984; 49 U. S. C. 425 (a). Interpret or apply secs. 601-610, 52 Stat. 1007-1012, 62 Stat. 1216; 49 U. S. C. 551-560, act of July 1, 1948)

Dated: March 8, 1951, at Washington, D. C.

By the Bureau of Safety Regulation.

[SEAL] JOHN M. CHAMBERLAIN,
*Director.*

[F. R. Doc. 51-3218; Filed, Mar. 12, 1951; 8:52 a. m.]

## INTERSTATE COMMERCE COMMISSION

### [ 49 CFR, Part 400 ]

CONTRACTS BETWEEN FREIGHT FORWARDERS AND MOTOR COMMON CARRIERS

NOTICE OF PROPOSED RULE MAKING

MARCH 5, 1951.

In the matter of rules and regulations for the filing of contracts covering service by motor common carriers for freight forwarders and the compensation to be paid therefor.

Notice is hereby given that the Commission has under consideration the prescription, under the authority of section 409 of the Interstate Commerce Act, as amended by Public Law 881 of the 81st Congress, of rules and regulations for the filing with the Commission of contracts between freight forwarders subject to part IV of that act and common carriers by motor vehicle subject to part II of that act, governing the utilization by such freight forwarders of the services and instrumentalities of such common carriers. The following suggested rules will be considered:

§ 400.1 *Filing.* All contracts, and amendments thereto, between freight forwarders and motor common carriers, entered into pursuant to section 409 of the Interstate Commerce Act, as amended December 20, 1950, and amendments to contracts continued, shall be in writing, and the freight forwarder party thereto shall file with the Interstate Commerce Commission three true copies thereof on paper of good quality, size 8½ x 11.

§ 400.2 *Specifications.* All such contracts and amendments shall show:

(a) In the upper right-hand corner a number in the consecutive series of the forwarder filing the same;

(b) The full and correct name and address of each party to the contract, and the ICC number, omitting subnumbers, identifying the operating authority of each;

(c) The points between which, or the territory from or to which, motor carrier service is to be performed under the contract, and the compensation to be paid therefor, stated in lawful moneys of the United States and separately as to each service or movement, and whether each service is assembling, distribution, or terminal-to-terminal service;

(d) The effective date of the contract; and

(e) All terms and conditions agreed upon between the parties to the contract.

§ 400.3 *Amendments.* Amendments to contracts shall show the same series number as the original contract, be consecutively numbered, and specifically indicate the provisions superseded; and where a contract is superseded by a new contract, the new contract shall specifically cancel the old contract.

§ 400.4 *Time of filing and notice of termination.* Contracts and amendments thereto shall be filed with the Commission within 10 days after the effective date thereof. Within 10 days after the effective date of termination of a contract, the forwarder party thereto shall file with the Commission three copies of a notice showing the effective date of such termination.

§ 400.5 *Contracts continued.* Evidence of agreements or amendments thereto, filed with the Commission prior to September 20, 1951, in accordance with the regulations heretofore proposed in Docket No. 29493, Freight forwarders, motor common carriers, agreements, 272 I. C. C. 413 (49 CFR Part 400), will be accepted as substantial compliance with the rules and regulations in this part, but any changes in such agreements with any carrier subsequent to September 20, 1951, shall be indicated by the filing, in conformity with the rules and regulations in this part, of complete new contracts covering service by that carrier, or of amendments completely covering the particular traffic involved, which amendments shall clearly indicate the portions of the schedules and evidence of concurrence superseded thereby; except that all such filings made prior to September 20, 1951, shall be superseded by new contracts complying with the rules and regulations in this part and filed with this Commission not later than December 31, 1952.

§ 400.6 *Public inspection.* All contracts and amendments thereto filed with the Commission under the rules and regulations in this part shall be open to public inspection.

§ 400.7 *Effective date.* The rules and regulations in this part shall become effective September 20, 1951.

Any interested party desiring to make representations in favor of or against the proposed rules and regulations or to suggest alternatives may do so through the submission of written data, views, or arguments. The original and 14 copies of such submission shall be filed with the Commission on or before April 12, 1951.

Notice will be given to the general public by posting copies hereof in the office of the Secretary of the Interstate Commerce Commission, Washington, D. C., and by filing with the Director of the Federal Register.

By the Commission.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3207; Filed, Mar. 12, 1951; 8:49 a. m.]

# NOTICES

## DEPARTMENT OF AGRICULTURE

### Forest Service

MODOC NATIONAL FOREST

REMOVAL OF TRESPASSING HORSES

Whereas a number of horses are trespassing and grazing on portions of the Modoc National Forest in the State of California; and

Whereas these horses are consuming forage needed for permitted livestock, are causing extra expense to established permittees, and are injuring national-forest lands;

Now, therefore, by virtue of the authority vested in the Secretary of Agriculture by the act of June 4, 1897 (30 Stat., 35; 16 U. S. C. 551), and the act of February 1, 1905 (33 Stat., 628; 16 U. S. C. 472), the following order is issued for the occupancy, use, protection, and administration of the Happy Camp, Doublehead, and Goose Lake Districts of the Modoc National Forest, within the boundaries described below:

*Temporary closure from livestock grazing.* (a) The grazing allotments described below are hereby closed for the period from April 1, 1951, to December 31, 1951, to the grazing of horses excepting those which are lawfully grazing on or crossing land in such allotments pursuant to the regulations of the Secretary of Agriculture, or which are used in connection with operations authorized by such regulations, or which are used as riding, pack, or draft animals by persons traveling over such land. The boundaries of the allotments are more particularly described as follows:

Commencing at the intersection of the Modoc National Forest boundary with the Oregon-California State line at the NW corner, Sec. 13, T. 48 N., R. 6 E., M. D. M.;

Thence easterly along the Oregon-California State line to its intersection with the boundary of the Modoc National Forest in Sec. 21, T. 48 N., R. 13 E., M. D. M.;

Thence southerly along the boundary of the Modoc National Forest to the section corner common to Sections 15, 16, 21 and 22, T. 43 N., R. 13 S., M. D. M., approximately one mile east of Griener Reservoir;

Thence westerly and southerly along the boundary of Modoc National Forest to the section corner common to Sections 9, 10, 15, and 16, T. 41 N., R. 9 E., M. D. M.;

Thence northeasterly along the road intersecting Highway No. 299 adjacent to and north of Pit River; through Pit River Guard Station, Turner Creek, Cottonwood Flat, Craig Spring, McCay (cabin) to intersection with the Lookout road approximately one mile east of Upper Mud Lake;

Thence northerly along latter road to intersection with Canby-Tule Lake highway near Cannon Reservoir;

Thence northwest along Canby-Tule Lake highway to intersection near Flukey Spring (south of Perez) with main traveled road to Lava Beds National Monument;

Thence westerly along latter road via Mammoth Cave to south of Little Sand Butte to the survey corner common to Townships 44 and 45 North, Ranges 4 and 5 East, M. D. M., at the Siskiyou-Modoc County line;

Thence north along said county line approximately six miles to township line; east one-half mile; and north two miles between Sections 30, 31, 29, 32 to the survey corner common to Sections 19, 20, 29, and 30, T. 46 N., R. 5 E., M. D. M., at intersection with the boundary of Modoc National Forest;

Thence easterly and northerly along said Forest boundary to point of commencement at the Oregon-California State line.

(b) Forest officers are hereby authorized to dispose of, in the most humane manner, all horses found trespassing or grazing in violation of this order.

(c) Public notice of intention to dispose of such horses shall be given by posting notices in public places or advertising in a newspaper of general circulation in the locality in which the Modoc National Forest is located.

Done at Washington, D. C., this 7th day of March 1951.

[SEAL] K. T. HUTCHINSON, *Acting Secretary of Agriculture.*

[F. R. Doc. 51-3193; Filed, Mar. 12, 1951; 8:46 a. m.]

### Production and Marketing Administration

[P. & S. Docket No. 383]

ST. LOUIS NATIONAL STOCK YARDS

NOTICE OF PETITION FOR MODIFICATION

In re: Market Agencies at St. Louis National Stock Yards, respondents.

Pursuant to the provisions of the Packers and Stockyards Act, 1921, as amended (7 U. S. C. 181 et seq.), an order was issued on March 23, 1949 (8 A. D. 254), authorizing assessment of the rates presently in effect for a period of one year beginning April 1, 1949. Subsequently, by an order dated February 9, 1950 (9 A. D. 202), the authorization was continued in effect to and including September 30, 1951.

On February 26, 1951, a petition was filed on behalf of respondents, requesting that an order be issued authorizing the market agencies (respondents) to assess the following selling and buying commissions:

SELLING CHARGES

| | Per head |
|---|---|
| Cattle: | |
| Consignments of one head and one head only | $1.30 |
| Consignments of more than one head: | |
| First 5 head in each consignment | 1.10 |
| Next 10 head in each consignment | 1.00 |
| Each head over 15 in each consignment | .95 |
| Calves: | |
| Consignments of one head and one head only | .75 |
| Consignments of more than one head: | |
| First 5 head in each consignment | .60 |
| Next 10 head in each consignment | .50 |
| Each head over 15 in each consignment | .40 |
| Bulls: | |
| Bulls irrespective of the number in a consignment | 1.65 |
| TB or bangs reactor cattle and calves irrespective of weight | 1.65 |
| Suspects or condemned cattle and calves | 1.65 |
| Hogs: | |
| Consignments of one head and one head only | .55 |
| Consignments of more than one head: | |
| First 10 head in each consignment | .39 |
| Next 15 head in each consignment | .34 |
| Each head over 25 in each consignment | .29 |
| Sheep: | |
| Consignments of one head and one head only | .50 |
| Consignments of more than one head: | |
| First 10 head in each 240 head in each consignment | .37 |
| Next 50 head in each 240 head in each consignment | .24 |
| Next 60 head in each 240 head in each consignment | .14 |
| Next 120 head in each 240 heads in each consignment | .09 |

MAXIMUM CHARGES

The maximum selling charge on any one rail consignment of sheep shall not exceed an amount equal to $20 multiplied by the number of single-deck cars in the consignment plus an amount equal to $30 multiplied by the number of double-deck cars in the consignment.

SECTION C—RESALES

| | Per head |
|---|---|
| Bulls | $1.65 |
| Cattle | .90 |
| Calves | .45 |
| Hogs | .29 |
| Sheep | .25 |

SECTION E—EXTRA SERVICE CHARGES

| | |
|---|---|
| Each weight draft in excess of one necessary to handle sold livestock in the best interest of the owner, or requested by him | $0.10 |

NOTE: On purchased livestock no draft charge applies.

MAXIMUM CHARGES—Continued

SECTION E—EXTRA SERVICE CHARGES—continued

| | |
|---|---|
| Each additional check, each additional copy of account sales, each proceeds deposit or bank credit over 1 | $0.10 |

BUYING

Cattle for immediate slaughter: Per head, same as selling rates.

MAXIMUM CHARGES

The maximum charge on any purchase order of cattle for immediate slaughter shipped out by rail shall not exceed an amount equal to $35 multiplied by the number of cars in which the order is shipped out.

If authorized, the modifications will produce additional revenues for respondents and increase the cost of marketing to shippers. Accordingly, it appears that this notice of the filing of the petition and its contents should be given to the public in order that all interested persons may have an opportunity to be heard in the matter.

All interested persons who desire to be heard in the matter shall notify the Hearing Clerk, United States Department of Agriculture, Washington 25, D. C., within 15 days from the date of publication of this notice.

Done at Washington, D. C., this 8th day of March 1951.

[SEAL] KATHERINE L. MASON,
*Hearing Clerk.*

[F. R. Doc. 51-3239; Filed, Mar. 12, 1951; 8:56 a. m.]

## DEPARTMENT OF COMMERCE

### Federal Maritime Board

[No. M-24]

COASTWISE LINE

NOTICE OF HEARING ON APPLICATION TO BAREBOAT CHARTER DRY-CARGO VESSELS

Pursuant to section 3, Public Law 591, 81st Congress, notice is hereby given that an informal public hearing will be held at Washington, D. C., on March 19, 1951, at 10 o'clock a. m., in Room 4821 Department of Commerce Building, before the Federal Maritime Board, upon the application of Coastwise Line, to bareboat charter two Liberty type vessels for use in its Pacific Coast-Alaska service (with privilege to call at British Columbia ports).

The purpose of the hearing is to receive evidence with respect to whether such service is required in the public interest and is not adequately served, and with respect to the availability of privately owned American-flag vessels on reasonable conditions and at reasonable rates for use in such service.

All persons having an interest in this application will be given an opportunity to be heard if present.

Dated: March 7, 1951.

By order of the Federal Maritime Board.

[SEAL] A. J. WILLIAMS,
*Secretary.*

[F. R. Doc. 51-3236; Filed, Mar. 12, 1951; 8:55 a. m.]

[No. M-25]

ISTHMIAN STEAMSHIP CO.

NOTICE OF HEARING ON APPLICATION TO BAREBOAT CHARTER GOVERNMENT-OWNED, WAR-BUILT, DRY-CARGO VESSELS, FOR USE IN THE GULF INTERCOASTAL SERVICE

Pursuant to section 3, Public Law 591, 81st Congress, notice is hereby given that an informal public hearing will be held in Room 4821, Commerce Building, Washington, D. C., on March 29, 1951, at 10 o'clock a. m., before Examiner A. L. Jordan, upon the application of Isthmian Steamship Company to bareboat charter Government-owned, war-built, dry-cargo vessels, for use in the gulf intercoastal service.

The purpose of the hearing is to receive evidence with respect to whether the service for which such vessels are proposed to be chartered is required in the public interest and is not adequately served, and with respect to the availability of privately-owned American-flag vessels for charter on reasonable conditions and at reasonable rates for use in such service.

All persons having an interest in such application will be given an opportunity to be heard if present.

The parties may have oral argument before the examiner immediately following the close of the hearing in lieu of briefs, and the examiner will issue a recommended decision. Parties may have 7 days within which to file exceptions to or memoranda in support of the examiner's recommended decision, but the Board reserves the right to determine whether oral argument on exceptions will be granted or whether briefs in connection therewith will be received.

Dated: March 8, 1951.

By order of the Federal Maritime Board.

[SEAL] A. J. WILLIAMS,
*Secretary.*

[F. R. Doc. 51-3267; Filed, Mar. 12, 1951; 8:59 a. m.]

## FEDERAL COMMUNICATIONS COMMISSION

[Docket No. 9886]

DOWLANDER BROADCASTING CO. (WOOF)

ORDER CONTINUING HEARING

In re application of R. A. Dowling, tr/as Dowlander Broadcasting Company (WOOF), Dothan, Alabama, Docket No. 9886, File No. BP-7757, for construction permit.

The Commission having under consideration a petition filed February 26, 1951 by R. A. Dowling, tr/as Dowlander Broadcasting Company, Dothan, Alabama, requesting that the hearing herein be continued for a period of sixty days from its presently scheduled date of March 7, 1951, in order that applicant's newly hired consulting engineer may complete engineering work in connection with the hearing; and

It appearing that both Counsel for Station WQAM, Miami, Florida, party respondent to this proceeding, and the General Counsel have consented to immediate action on the petition and indicated no objection to a grant thereof, thereby meeting the requirements of § 1.745 of the Commission's rules, and that good cause has been shown for a grant thereof;

*It is therefore ordered,* This 2d day of March 1951, that the petition of Dowlander Broadcasting Company (WOOF) be and it is hereby granted and the hearing herein is hereby continued to May 7, 1951, at 10:00 a. m., in Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3209; Filed, Mar. 12, 1951; 8:50 a. m.]

[Docket Nos. 9615, 9616]

VALLEY BROADCASTING CO. (KLOK) AND CHARLES E. SALIK (KCBQ)

ORDER SCHEDULING HEARING AND AMENDING ISSUES

In re applications of E. L. Barker, Claribel Barker, T. H. Canfield and Opal A. Canfield, d/b as Valley Broadcasting Company (KLOK), San Jose, California, Docket No. 9615, File No. BP-7400, for construction permit; Charles E. Salik (KCBQ), San Diego, California, Docket No. 9616, File No. BML-1392, for modification of license.

At a session of the Federal Communications Commission, held at its offices in Washington, D. C., on the 28th day of February 1951;

The Commission having under consideration a petition filed on November 6, 1950, by Valley Broadcasting Company requesting reconsideration and grant without hearing of its above-entitled application for construction permit as amended, to change power and hours of operation of Station KLOK, San Jose, California, from 5 kilowatts, daytime only to 1 kilowatt, 5 kilowatts-LS, unlimited time, and install directional antenna for night use only;

It appearing, that the said application originally requested power of 5 kilowatts, unlimited time employing directional antenna nights and was designated for hearing by Commission order of March 28, 1950, in a consolidated proceeding with the above-entitled application of Charles E. Salik for modification of license of Station KCBQ, San Diego, California, to increase nighttime power from 1 kilowatt to 5 kilowatts; and

It further appearing, that the petition of Valley Broadcasting Company filed on November 6, 1950, requesting leave to amend its above-entitled application to request power of 5 kilowatts day, 1 kilowatt night was granted on November 17, 1950, and that, as amended, the said application would not involve objectionable interference with any existing broadcast stations, but that objectionable interference may be involved nighttime with the above-entitled application of Charles E. Salik which would result in a nighttime limitation to petitioner's proposed operation greatly in excess of the 2.5

mv/m contour recommended in the Standards of Good Engineering Practice; and

It further appearing, that the operation of Station KLOK as proposed in the above-entitled application may not be in compliance with the Standards of Good Engineering Practice particularly with reference to nighttime service to the San Jose, California, metropolitan district and to the ratio of the population residing between the 2.5 mv/m normally protected and nighttime interference free contours to the population residing within the nighttime interference free contour and that nighttime service of Station KLOK operating as proposed may be degraded from the operation of Station KCBQ as proposed in the above-entitled application to increase nighttime power to an extent which in and of itself would prohibit a grant of both the above-entitled applications; and

It further appearing, that, in view of the above matters, the Commission cannot determine whether a grant of the said application of Valley Broadcasting Company would serve public interest, convenience, or necessity;

*It is ordered*, That the said petition is denied and that hearing on the above-entitled applications shall commence at 10:00 a. m. on April 30, 1951, at Washington, D. C.; and

*It is further ordered*, That, on the Commission's own motion, the order of March 28, 1950, designating the above-entitled applications for hearing in a consolidated proceeding is amended to renumber issues 3, 4, 5, and 6 as issues 4, 5, 6, and 7, respectively, and to include therein as issue 3 the following issue:

3. To determine the areas and populations which may be expected to gain or lose primary service from the operation of Stations KLOK and KCBQ as proposed, and the character of other broadcast service available to such areas and populations.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3210; Filed, Mar. 12, 1951; 8:50 a. m.]

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[Docket No. 9885]

LAWRENCE COUNTY BROADCASTING CO.

ORDER CONTINUING HEARING

In re application of James L. Harrison, J. E. Sowell, Harold Twitty and R. C. Wiley, d/b as Lawrence County Broadcasting Company, Lawrenceburg, Tennessee, Docket No. 9885, File No. BP-7756, for construction permit.

The Commission having under consideration a petition filed on February 23, 1951, by James L. Harrison, J. E. Sowell, Harold Twitty and R. C. Wiley, d/b as Lawrence County Broadcasting Company, Lawrenceburg, Tennessee, requesting that the hearing now scheduled to be held on March 2, 1951, be continued for a period of sixty days; and

It appearing, that no opposition has been filed to the above petition by any of the parties to this proceeding;

*It is ordered*, This 1st day of March 1951, that the petition be, and it is hereby granted; and that the hearing on the above-entitled application be, and it is hereby, continued to 10:00 a. m., Wednesday, May 2, 1951, at Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3211; Filed, Mar. 12, 1951; 8:50 a. m.]

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[Docket No. 9891]

RADIOMARINE CORP. OF AMERICA

ORDER CONTINUING HEARING

In the matter of Radiomarine Corporation of America, Docket No. 9891; charges, classifications, regulations and practices, for and in connection with Ship/Shore Radiotelephone Service via foreign coastal stations.

The Commission having under consideration a motion filed February 28, 1951, by the Chief, Common Carrier Bureau, Federal Communications Commission, requesting indefinite continuance of the hearing on the above-entitled proceeding presently scheduled for March 12, 1951, pending action by the Commission upon application for special tariff permission filed by Radiomarine Corporation of America on February 26, 1951; and

It appearing, that said application requests authority to cancel the tariff schedules which are the subject of suspension and investigation in this proceeding; and if such application is granted and the tariff schedules are cancelled pursuant thereto the proceeding may become moot; and

It further appearing, that other counsel in the proceeding have informally consented to a waiver of § 1.745 of the Commission's rules to permit the early consideration and grant of the motion for continuance;

*It is ordered*, This 2d day of March 1951, that the petition be, and it is hereby, granted; and the hearing on the above-entitled application be, and it is hereby, continued until further order.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3212; Filed, Mar. 12, 1951; 8:50 a. m.]

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[Docket Nos. 9179, 9575]

SPA BROADCASTERS, INC., AND SARATOGA BROADCASTING CO.

ORDER SCHEDULING FURTHER HEARING

In re applications of Spa Broadcasters, Inc., Saratoga Springs, New York, Docket No. 9179, File No. BP-6808; Saratoga Broadcasting Company, a partnership composed of John Nazak and Joanne May Levko, Saratoga Springs, New York, Docket No. 9575, File No. BP-7459, for construction permits.

Pursuant to the Commission's memorandum opinion and order issued on February 7, 1951, denying a petition filed on behalf of Spa Broadcasters, Inc., Saratoga Springs, New York, to reconsider and set aside the Commission's memorandum opinion and order of August 17, 1950, in which the Commission ordered that the record in the above-entitled proceeding be reopened to permit the Saratoga Broadcasting Company, Saratoga Springs, New York, to present evidence in support of its application (Docket No. 9575).

*It is ordered*, This 2d day of March 1951, that a further hearing in the above-entitled proceeding is scheduled to be held in Washington, D. C., at 10:00 a. m., on Wednesday, April 4, 1951.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3213; Filed, Mar. 12, 1951; 8:51 a. m.]

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[Docket Nos. 9894-9896, 9912]

BOOTH RADIO & TELEVISION STATIONS, INC., ET AL.

ORDER CONTINUING HEARING

In re applications of Booth Radio & Television Stations, Inc., Lansing, Michigan, Docket No. 9894, File No. BP-7905; John C. Pomeroy, Pontiac, Michigan, Docket No. 9895, File No. BP-7811; Adelaide Lillian Carrell, Flint, Michigan, Docket No. 9896, File No. BP-7840; Oakland Broadcasting Company, Pontiac, Michigan, Docket No. 9912, File No. BP-7984, for construction permits.

The Commission having under consideration a petition filed February 23, 1951, by Booth Radio and Television Stations, Inc., Lansing, Michigan, requesting a continuance of the hearing from March 22, 1951, to May 14, 1951, in the proceeding upon the above-entitled applications for construction permits; and an opposition thereto filed on February 27, 1951, by Adelaide Lillian Carrell; and

It appearing, that the remaining parties in this proceeding have not objected to a continuance of the hearing; that this is the first request for a continuance in this proceeding; and that in view of the illness of the principal stockholder of Booth Radio and Television Stations, Inc. the continuance sought is reasonable;

*It is ordered*, This 2d day of March 1951, that the petition is granted; and that the hearing in the above-entitled proceeding is continued to 10:00 a. m., Monday, May 14, 1951, at Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3214; Filed, Mar. 12, 1951; 8:51 a. m.]

[Docket No. 9893]

WARNER BROS. (KWBR)

ORDER CONTINUING HEARING

In re application of S. W. Warner and E. N. Warner d/b as Warner Brothers (KWBR), Oakland, California, Docket No. 9893, File No. BP-7709, for construction permit.

The Commission having under consideration a petition filed February 27, 1951, by S. W. Warner and E. N. Warner d/b as Warner Brothers (KWBR), Oakland, California, requesting a 90-day continuance of the hearing presently scheduled for March 16, 1951, at Washington, D. C., in the proceeding upon its above-entitled application for construction permit;

*It is ordered*, This 2d day of March 1951, that the petition is granted; and that the hearing in the above-entitled proceeding is continued to 10:00 a. m., Monday, June 18, 1951, at Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3215; Filed, Mar. 12, 1951; 8:51 a. m.]

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[Docket No. 9738]

WHARTON COUNTY BROADCASTING CO., INC. (KULP)

ORDER CONTINUING HEARING

In re application of Wharton County Broadcasting Company, Inc. (KULP), El Campo, Texas, Docket No. 9738, File No. BP-7644, for construction permit.

The Commission having under consideration a petition filed February 23, 1951, by Wharton County Broadcasting Company, Incorporated (KULP), El Campo, Texas, requesting reconsideration and rehearing of its above-entitled application; and

It appearing, that on January 29, 1951, the Commission denied a petition filed by Wharton County Broadcasting Company, Inc. (KULP) requesting a waiver of hearing pursuant to § 1.391 of the Commission's rules and regulations; and that the petitioner is apparently of the impression that the denial of its said petition for waiver of hearing has the effect of precluding hearing on its above-entitled application; and

It further appearing, that the Commission denied the said petition for rehearing inasmuch as it considered this to be an appropriate case for the presentation of oral testimony; that the petitioner is in effect only asking that it be afforded a hearing on its above-entitled application; that the petitioner is not seeking reconsideration or rehearing; and that, therefore, there is no need to act on this petition;

*It is ordered*, this 2d day of March 1951, that the petition for reconsideration and rehearing is dismissed; and that the hearing in the above-entitled proceeding is scheduled to be heard at 10:00 a. m., Friday, April 20, 1951, at Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3216; Filed, Mar. 12, 1951; 8:51 a. m.]

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[Docket No. 9587]

PRATT BROADCASTING CO.

ORDER CONTINUING HEARING

In re application of Clem Morgan and Robert E. Schmidt, d/b as Pratt Broadcasting Company, Pratt, Kansas, Docket No. 9587, File No. BP-7395, for construction permit.

The Commission having under consideration a petition filed February 27, 1951, by KVGB, Inc. (KVGB), Great Bend, Kansas, party respondent in the above-entitled proceeding, for a continuance to April 5, 1951, of the hearing in the above-entitled matter now scheduled for March 9, 1951; and

It appearing, that party respondent's consulting engineer will be unable to participate in the hearing on the date presently scheduled, and that another witness who may be called to testify on behalf of KVGB, Inc., is now en route to the Mayo Clinic at Rochester, Minnesota, assisting in the care and transportation of an associate, and will be unable to be in Washington on the presently scheduled hearing date; and

It further appearing, that the time within which opposition to this petition for continuance might be filed has expired and no such opposition has been filed by any party or by Commission counsel, and that good cause has been shown for the requested continuance;

*It is ordered*, This 5th day of March 1951, that the petition is granted, and the hearing on the above-entitled matter now scheduled for March 9, 1951, is continued to 10 o'clock a. m., April 5, 1951, in Washington, D. C.

FEDERAL COMMUNICATIONS COMMISSION,
[SEAL] T. J. SLOWIE,
*Secretary.*

[F. R. Doc. 51-3217; Filed, Mar. 12, 1951; 8:51 a. m.]

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## FEDERAL POWER COMMISSION

[Docket No. G-1556]

SOUTHERN CALIFORNIA GAS CO.

NOTICE OF ORDER APPROVING TRANSFERS OF AMOUNTS IN DEPRECIATION RESERVE

MARCH 7, 1951.

Notice is hereby given that, on March 5, 1951, the Federal Power Commission issued its order entered March 2, 1951, amending order issued February 13, 1951, published in the FEDERAL REGISTER on February 17, 1951 (16 F. R. 1690), in the above-designated matter.

[SEAL] LEON M. FUQUAY,
*Secretary.*

[F. R. Doc. 51-3208; Filed, Mar. 12, 1951; 8:49 a. m.]

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[Docket No. G-1612]

PANHANDLE EASTERN PIPE LINE CO.

NOTICE OF APPLICATION

MARCH 7, 1951.

Take notice that on February 15, 1951, Panhandle Eastern Pipe Line Company (Applicant), a Delaware corporation with its principal office at Kansas City, Missouri, filed an application in the alternative seeking (a) a disclaimer by the Commission of its jurisdiction or (b) a certificate of public convenience and necessity, pursuant to section 7 of the Natural Gas Act, as amended, authorizing the construction and operation of (1) approximately 400 feet of 6⅝-inch O. D. pipeline extending from Applicant's Quincy lateral in Marion County, Missouri, to a point of delivery on the property and with the facilities of the Northeast Missouri Electric Power Cooperative (Northeast Missouri) and (2) metering and regulating facilities for the direct sale of natural gas to Northeast Missouri.

Applicant proposes to construct and operate the described facilities for the purpose of selling natural gas to Northeast Missouri under the terms of a contract dated December 15, 1950, providing for the sale and delivery of natural gas in volumes not to exceed 1,200 Mcf daily on a "dump" basis, when Applicant has available gas in excess of its commitments to customers to whom gas is being sold on other than a temporary or dump basis.

Applicant states the facilities proposed are only incidental measuring facilities and, as such exempt from the jurisdiction of the Commission; that the proposed sale is not a sale for resale within the meaning of section 1 (b) of the Natural Gas Act.

The estimated cost of the facilities proposed to be constructed is approximately $5,000, which will be financed out of current funds.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the rules of practice and procedure (18 CFR 1.8 and 1.10) on or before the 27th day of March 1951. The application is on file with the Federal Power Commission for public inspection.

[SEAL] LEON M. FUQUAY,
*Secretary.*

[F. R. Doc. 51-3199; Filed, Mar. 12, 1951; 8:46 a. m.]

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[Docket No. G-1619]

EL PASO NATURAL GAS CO.

NOTICE OF APPLICATION

MARCH 7, 1951.

Take notice that on February 23, 1951, El Paso Natural Gas Company (Applicant), a Delaware corporation, of El Paso, Texas, filed an application for a certificate of public convenience and necessity pursuant to section 7 of the Natural Gas Act, authorizing the installation of a meter station, at a point on its main transmission system in Pinal County, Arizona. Applicant proposes by these facilities to sell and deliver natural

gas to Arizona Edison Company, Inc., for resale and distribution in the towns of Ray and Sonora, Arizona. These communities have no gas utility service at present.

Through the proposed facilities, Applicant expects to deliver a maximum of 68,000 Mcf per year with a daily maximum of about 585 Mcf of natural gas. The cost of these facilities is estimated to be $2,800, which will be paid from general funds of Applicant.

Applicant requests that its application be heard under the shortened procedure pursuant to § 1.32 (b) of the rules of practice and procedure.

Protests or petitions to intervene may be filed with the Federal Power Commission, Washington 25, D. C., in accordance with the rules of practice and procedure (18 CFR 1.8 or 1.10) on or before the 27th day of March 1951. The application is on file with the Commission for public inspection.

[SEAL] LEON M. FUQUAY,
*Secretary.*

[F. R. Doc. 51-3200; Filed, Mar. 12, 1951; 8:46 a. m.]

## FEDERAL RESERVE SYSTEM

### VOLUNTARY CREDIT RESTRAINT

### REQUEST TO FINANCING INSTITUTIONS

This "Request" is addressed to all financing institutions in the United States, including without limitation all individuals, firms, partnerships, corporations and other organizations of any kind which are engaged in the business of extending credit, making loans, or purchasing, discounting, selling, distributing, dealing in, or underwriting securities, any and all of such institutions being hereinafter referred to as "financing institutions".

Pursuant to the provisions of section 708 of the Defense Production Act of 1950 (hereinafter called the "act") and of section 701 of Executive Order No. 10161, the Board of Governors of the Federal Reserve System has consulted with representatives of financing with a view to encouraging the making of voluntary agreements and programs to further the objectives of the act. As a result of such consultations, such representatives have prepared a "Program for Voluntary Credit Restraint", including as a part thereof a Statement of Principles, the entire document being hereinafter referred to as the "Program". The Program is set forth below.

The Board of Governors of the Federal Reserve System hereby approves the Program and finds the Program to be in the public interest as contributing to the national defense. Under section 708 of the act and section 701 of the said order, acts or omissions to act pursuant to this Request and the Program which occur while said section 708 is in effect and before the withdrawal of this Request or of the finding of the Board in the preceding sentence are not construed to be within the prohibitions of the antitrust laws or the Federal Trade Commission Act of the United States.

The Board of Governors of the Federal Reserve System has consulted with the Attorney General and with the Chairman of the Federal Trade Commission on and before February 5, 1951, said date being not less than 10 days before the date of this Request, with regard to the provisions of the Program, the finding by the Board above mentioned and this Request; and the Attorney General has given his approval to the making of this Request.

Every financing institution in the United States is hereby requested by the Board of Governors of the Federal Reserve System to act, and to refrain from acting, pursuant to and in accordance with the provisions of the Program. The national committee which is to be set up pursuant to the provisions of the Program, each and every subcommittee set up pursuant to the provisions of the Program, and each and every individual who may become a member of said national committee or of any of said subcommittees are hereby requested by the Board of Governors of the Federal Reserve System to act, and to refrain from acting, pursuant to and in accordance with the provisions of the Program.

By order of the Board of Governors of the Federal Reserve System this 9th day of March 1951.

[SEAL] S. R. CARPENTER,
*Secretary.*

### PROGRAM FOR VOLUNTARY CREDIT RESTRAINT

#### PREAMBLE

The task of restraining strong inflationary pressures is one of the most difficult and most important in the whole range of economic problems today.

One part of this task—the restraint of unnecessary credit expansion—presents a challenge to the financing institutions throughout the nation.

Section 708 of the Defense Production Act of 1950 authorizes the President to encourage financing institutions to enter into voluntary agreements and programs to restrain credit, which will further the objectives of that act. By executive order, the President has delegated to the Board of Governors of the Federal Reserve System his authority with respect to financing under this section of the act upon the required condition that it consult with the Attorney General and with the Chairman of the Federal Trade Commission, and that it obtain the approval of the Attorney General before requesting actions under such voluntary agreements and programs.

At the invitation of the Board, and in company with it, representatives of the American Bankers Association, the Life Insurance Association of America and the Investment Bankers Association of America have been examining the possibilities of this method of credit restraint.

While it is recognized that the proposed Program is addressed only to one limited source of inflationary pressure, the vital importance of this problem to the stability of the economy, and the necessity to extend credit only in such a way as to restrain inflationary pressures outside the financing of the defense program should be emphasized to all financing institutions.

It is appropriate to point out that this Program of voluntary credit restraint does not have to do with such factors as inflationary lending by federal agencies, unnecessary spending, federal, state or local, and the wage-price spiral and other much more seriously contributing factors. These should be vigorously dealt with at the proper places. It assumes that the proper governmental authorities will exercise the requisite fiscal and monetary controls.

#### DEFINITIONS

As used herein:

The terms "financing institution" or "financing institutions" mean banks, life insurance companies, investment bankers engaged in the underwriting, distribution, dealing or participating, as agents or otherwise, in the offering, purchase or sale of securities, and such other types or groups of financial institutions as the Board of Governors of the Federal Reserve System may invite to participate in the Program.

The terms "loan", "loans", "lending" and "credit", in addition to their ordinary connotations, mean the supplying of funds through the underwriting and distribution of securities (either on a firm commitment, agency or "best efforts" basis), the making or assisting in the making of direct placements, or otherwise participating in the offering or distribution of securities.

#### STATEMENT OF PRINCIPLES

Pursuant to the provisions of section 708 (a) of the Defense Production Act of 1950, and with the approval of the Board of Governors of the Federal Reserve System in accordance with the functions delegated to it by section 701 (a) (2) of Executive Order 10161, this Statement of Principles has been drafted to which all financing institutions are asked to conform.

It shall be the purpose of financing institutions to extend credit in such a way as to help maintain and increase the strength of the domestic economy through the restraint of inflationary tendencies and at the same time to help finance the defense program and the essential needs of agriculture, industry and commerce.

Inflation may be defined as a condition in which the effective demand for goods and services exceeds the available supply, thus exerting an upward pressure on prices.

Any increase in lending at a more rapid rate than production can be increased exerts an inflationary influence. Under present conditions of very high employment of labor, materials and equipment, the extension of loans to finance increased output will have an initial inflationary effect; but loans which ultimately result in a commensurate increase in production of an essential nature are not inflationary in the long run whatever their temporary effect may be. It is most important, however, that loans for nonessential purposes be curtailed in order to release some of the nation's resources for expansion in more vital areas of production.

Cooperation with this program of credit restraint makes it increasingly necessary for financing institutions to screen loan applications on the basis of their purpose, in addition to the usual tests of credit worthiness. The criterion for sound lending in a period of inflationary danger boils down to the following: Does it commensurately increase or maintain production, processing and distribution of essential goods and services?

In interpretation of the foregoing, the following types of loans would be classified as proper:

1. Loans for defense production, direct or indirect, including fuel, power, and transportation.

2. Loans for the production, processing and orderly distribution of agricultural and other staple products, including export and import as well as domestic, and of goods and services supplying the essential day-to-day needs of the country.

3. Loans to augment working capital where higher wages and prices of materials make such loans necessary to sustain essential production, processing or distribution services.

4. Loans to securities dealers in the normal conduct of their business or to them or others incidental to the flotation and distribution of securities where the money is being raised for any of the foregoing purposes.

This Program would not seek to restrict loans guaranteed or insured, or authorized as to purpose by a Government agency, on the theory that they should be restricted, in accordance with national policy, at the source of guaranty or authorization. Financing institutions would not be restricted in honoring previous commitments.

The following are types of loans which in general financing institutions should not make under present conditions, unless modified by the circumstances of the particular loan so as not to be inconsistent with the principles of this Program:

1. Loans to retire or acquire corporate equities in the hands of the public, including loans for the acquisition of existing companies or plants where no overall increase of production would result.

2. Loans for speculative investments or purchases. The first test of speculation is whether the purchase is for any purpose other than use or distribution in the normal course of the borrower's business. The second test is whether the amounts involved are disproportionate to the borrower's normal business operations.[1] This would include speculative expansion of real estate holdings or plant facilities as well as speculative accumulation of inventories in expectation of resale instead of use.

The foregoing principles should be applied in screening as to purpose on all loans on securities whether or not covered by Regulations U or T.

[1] Loans additional to those needed for a borrower's normal business may, of course, be regarded as proper when they are for the purpose of defense production or otherwise conform to the types of loans listed as proper in this Statement of Principles.

Recognizing that the maximum estimate of the percentage of our 1951 production which will be devoted directly or indirectly to national defense is between 20 percent and 30 percent, a very substantial proportion of the lending of the country will be devoted to the financing of the production and growth of our industrial and commercial community. In these circumstances, it is felt that each financing institution can help accomplish the objectives outlined above by careful screening of each application for credit extension.

In carrying out such screening, financing institutions should not only observe the letter of the existing regulations of the Board of Governors of the Federal Reserve System with respect to real estate credit, consumer credit, security loans, etc., but should also apply to all their lending the spirit of these and such other regulations and guiding principles as the Government may from time to time announce in the fight against inflation.

This Program is necessarily very general in nature. It is a voluntary Program to aid in the over-all efforts to restrain inflation. To be helpful, this Program must rely on the good will of all financing institutions and the over-all intention to comply with its spirit.

PROCEDURE FOR IMPLEMENTING THE PROGRAM

Pursuant to the provisions of section 708 (b) and (c) of the Defense Production Act of 1950, and upon full compliance with the terms and conditions thereof:

1. A "Voluntary Credit Restraint Committee" (hereinafter referred to as "the Committee") will be appointed by the Board of Governors of the Federal Reserve System (hereinafter referred to as "the Board"). Members shall be appointed for such terms as the Board may prescribe. Initially, the Committee will consist of twelve members, four representing the life insurance companies, four representing the investment bankers, and four representing the banks. The membership of the Committee may from time to time be expanded as deemed advisable or appropriate by the Board to insure adequate representation thereon of other types or groups of financing institutions which may participate in the Program. In selecting and appointing the members of the Committee, the Board shall have due regard to fair representation thereon for small, for medium and for large financing institutions, and for different geographical areas. The Committee will:

(a) With such assistance from the Board and the Federal Reserve Banks as may be necessary, distribute this statement of the Program, including the Statement of Principles, to financing institutions to such extent as may be deemed desirable in view of any distribution previously made;

(b) Appoint the subcommittees referred to below in 2;

(c) Meet for the purpose of considering the functioning of the Program, advising the Board with respect thereto, and suggesting for the consideration of the Board such changes in the Program, including the Statement of Principles, as may from time to time appear appropriate. Meetings of the Committee shall be held at the call of an official of the Federal Reserve System, designated by the Board; shall be under the chairmanship of such an official; and an agenda for such meetings shall be prepared by such an official. Full and complete minutes of each meeting shall be made by such an official and copies shall be kept in the files of the Board available for public inspection.

2. Subcommittees may be established for each type of financing institution participating in the Program. One of the members of each subcommittee located in any city in which there is a Federal Reserve Bank or branch thereof will be a Federal Reserve representative designated by the Board of Governors of the Federal Reserve System or by such Federal Reserve Bank or branch; and such member shall attend each meeting of the subcommittee. For the investment bankers, the life insurance companies, and the banks there may in each case be one or more subcommittees organized. All such subcommittees will meet only for the purposes specified in the Program; will maintain records of their actions; and will make reports directly to the Committee regarding the actions taken by them, including statements of the types of cases considered and the nature of the advice given. The subcommittees will be available for consultation with individual financing institutions to assist them in determining the application of the Statement of Principles with respect to specific loans for which application has been made to such financing institutions. In consulting with a subcommittee, a financing institution shall not be required to disclose the identity of the applicant for any loan. No financing institution shall be required to consult with any subcommittee with respect to any loan or loans, or any application or applications therefor. Consultation with a subcommittee shall be wholly within the individual and independent discretion of a financing institution. The final decision with respect to making or refusing to make any particular loan or loans shall likewise remain wholly within the individual and independent discretion of each financing institution, whether or not it has consulted with any of the subcommittees.

In setting up the subcommittees, the Committee shall have due regard for fair representation thereon for small, for medium and for large financing institutions, and for different geographical areas. It shall also inform the Board of all subcommittee appointments.

3. The Committee shall be furnished with such compilations of statistical data on extension of credit by financing institutions as may be required to show the amounts and direction of credit use and to watch the operation of the Program. Such statistics shall be compiled by the Board. To assist the Board in making such compilations, data shall be supplied for the investment bankers, jointly by the Investment Bankers Association and the National Association of Securities Dealers, and for the life insurance companies, jointly by the Life Insurance Association of America and the American

Life Convention. Compilations of data made by the Board shall not reveal the identity of individual financing institutions or borrowers. Such compilations shall be kept on file with the Board and shall be available for public inspection.

4. Financing institutions participating in the Program will keep records of individual loans, as to purpose, in such form as to be available for future analysis.

5. Any change in the Program, including the Statement of Principles, shall be passed upon by the Committee and shall be made in accordance with the requirements of section 708 of the Defense Production Act of 1950.

All actions pursuant to and under the Program will be automatically terminated by all participating financing institutions as of the termination of the authority conferred under section 708 of the Defense Production Act of 1950; or upon withdrawal by the Board of its request for action under the Program. If the Committee, after study of the operation of the Program, concludes that it is no longer necessary or is not making a substantial contribution to the solution of the problem for which the Program was established, it shall so advise the Board.

[F. R. Doc. 51-3286; Filed, Mar. 9, 1951; 5:04 p. m.]

## INTERSTATE COMMERCE COMMISSION

[4th Sec. Application 25892]

SULPHURIC ACID FROM EAST ST. LOUIS, ILL., AND ST. LOUIS, MO., TO DAVIS, MISS.

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: D. Q. Marsh, Agent, for Missouri Pacific Railroad Company, St. Louis-San Francisco Railway Company and St. Louis Southwestern Railway Company pursuant to fourth section order No. 16101.

Commodities involved: Sulphuric acid, in tank-car loads.

From: East St. Louis, Ill., and St. Louis, Mo.

To: Davis, Miss.

Grounds for relief: Circuitous routes and operation through higher-rated territory.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3201; Filed, Mar. 12, 1951; 8:47 a. m.]

[4th Sec. Application 25893]

CLASS RATES BETWEEN OFFICIAL TERRITORY AND EASTERN CANADA

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: C. W. Boin and L. C. Schuldt, Agents, for carriers parties to Agent C. W. Boin's tariff I. C. C. No. A-721 and Agent L. C. Schuldt's tariff I. C. C. No. 3814.

Involving: Class rates.

Between: Points in official territory and points in eastern Canada generally north of Montreal and west of Megantic and Levis, Que.

Grounds for relief: Circuitous routes.

Schedules filed containing proposed rates: C. W. Boin's tariff I. C. C. No. A-721, Supp. 78; L. C. Schuldt's tariff I. C. C. No. 3814, Supp. 48.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3202; Filed, Mar. 12, 1951; 8:47 a. m.]

[4th Sec. Application 25894]

LOGS FROM HARRODSBURG, KY., TO SMYRNA, TENN.

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: R. E. Boyle, Jr., Agent, for Louisville and Nashville Railroad Company, The Nashville, Chattanooga & St. Louis Railway and Southern Railway Company.

Commodities involved: Logs, native wood, carloads.

From: Harrodsburg, Ky.

To: Smyrna, Tenn.

Grounds for relief: Circuitous routes.

Schedules filed containing proposed rates: C. A. Spaninger's tariff I. C. C. No. 890, Supp. 177.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3203; Filed, Mar. 12, 1951; 8:48 a. m.]

[4th Sec. Application 25895]

PIG IRON FROM DAINGERFIELD AND LONE STAR, TEX., TO POINTS IN WISCONSIN

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: D. Q. Marsh, Agent, for carriers parties tariff to his I. C. C. No. 3599.

Commodities involved: Pig iron, carloads.

From: Daingerfield and Lone Star, Tex.

To: Points in Wisconsin.

Grounds for relief: Competition with rail carriers and circuitous routes.

Schedules filed containing proposed rates: D. Q. Marsh's tariff I. C. C. No. 3599, Supp. 74.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary

relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3204; Filed, Mar. 12, 1951; 8:48 a. m.]

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[4th Sec. Application 25896]

ETHYLENE GLYCOL FROM PORT NECHES, TEX., TO CLEVELAND, OHIO, AND LATROBE, PA.

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: D. Q. Marsh, Agent, for carriers parties to his tariff I. C. C. No. 3721.

Commodities involved: Ethylene glycol, in tank-car loads.

From: Port Neches, Tex.

To: Cleveland, Ohio, and Latrobe, Pa.

Grounds for relief: Competition with rail carriers and circuitous routes.

Schedules filed containing proposed rates: D. Q. Marsh's tariff I. C. C. No. 3721, Supp. 171.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3205; Filed, Mar. 12, 1951; 8:48 a. m.]

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[4th Sec. Application 25897]

MANGANESE FROM EMCO, ALA., TO HOUSTON, TEX.

APPLICATION FOR RELIEF

MARCH 8, 1951.

The Commission is in receipt of the above-entitled and numbered application for relief from the long-and-short-haul provision of section 4 (1) of the Interstate Commerce Act.

Filed by: D. Q. Marsh, Agent, for carriers parties to his tariff I. C. C. No. 3899.

Commodities involved: Ferro-manganese, ferro-silicon, silico-manganese and zirconium-ferro-silicon, carloads.

From: Emco, Ala.

To: Houston, Tex.

Grounds for relief: Circuitous routes.

Schedules filed containing proposed rates: D. Q. Marsh's tariff I. C. C. No. 3899, Supp. 37.

Any interested person desiring the Commission to hold a hearing upon such application shall request the Commission in writing so to do within 15 days from the date of this notice. As provided by the general rules of practice of the Commission, Rule 73, persons other than applicants should fairly disclose their interest, and the position they intend to take at the hearing with respect to the application. Otherwise the Commission, in its discretion, may proceed to investigate and determine the matters involved in such application without further or formal hearing. If because of an emergency a grant of temporary relief is found to be necessary before the expiration of the 15-day period, a hearing, upon a request filed within that period, may be held subsequently.

By the Commission, Division 2.

[SEAL] W. P. BARTEL, *Secretary.*

[F. R. Doc. 51-3206; Filed, Mar. 12, 1951; 8:49 a. m.]

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## SECURITIES AND EXCHANGE COMMISSION

[File No. 54-184]

UNITED CORP.

ORDER MAKING LIST OF STOCKHOLDERS AVAILABLE FOR INSPECTION

At a regular session of the Securities and Exchange Commission, held at its office in the city of Washington, D. C., on the 5th day of March A. D. 1951.

Randolph Phillips, a common stockholder of the United Corporation and Chairman of the Committee for the Common Stockholders of the United Corporation, having filed a petition requesting that the Commission: (1) Direct United to include in its solicitation material for the 1951 annual stockholders' meeting the names of two nominees of the Committee among the seven nominees for directors for whom proxies are to be solicited; (2) find that any board of directors of United which includes directors originally nominated to represent the preferred stock would be unrepresentative and contrary to the standards of sections 11 (b) (2) and 12 (e) of the Public Utility Holding Company Act of 1935; (3) find that the incumbent board is unrepresentative since it excludes representatives of the 22,000 stockholders who voted against the board; (4) take steps for the enforcement of cumulative voting in time to be effective for the 1951 annual meeting; (5) direct United to mail proxy forms furnished by petitioner to United's common stockholders; (6) direct United to make available to petitioner stockholders' lists; (7) direct United to appoint as inspectors of election at the 1951 meeting one person designated by the management and one by opposition stockholders; (8) if it denies the relief requested to include two nominees of the Committee among the seven nominees for directors, prohibit United from expending any funds for proxy solicitation to elect the three nominees of the management opposed by petitioner and the Committee;

United having filed an answer to the petition opposing the granting of any of the relief requested by Phillips;

Phillips having filed certain solicitation material pursuant to Regulation X-14 promulgated under the Securities Exchange Act of 1934 under which regulation a procedure is available to petitioner pursuant to Rule X-14A-7 for securing the mailing of the material by the company;

A plan having been filed by United under section 11 (e) of the Holding Company Act, hearings thereon having been concluded, briefs filed and oral argument held, the Commission having taken the matter under advisement, and the said petition appearing in the main to request summary action, in advance of a determination of the issues in the section 11 (e) proceeding, granting relief of similar nature to that requested by petitioner in that proceeding;

The Commission having not as yet reached a determination of the issues in the section 11 (e) proceeding and being of the opinion, under all the circumstances, that such interim summary relief is not appropriate in the public interest;

*It is ordered,* That United make available at its New York office for inspection by petitioner and his representatives a list of all the common stockholders of record as of the close of business on the record date selected for voting at the 1951 annual meeting, including the address of and number of shares owned by each such holder; and

*It is further ordered,* That in all other respects the said petition be and it is hereby denied.

By the Commission.

[SEAL] ORVAL L. DUBOIS, *Secretary.*

[F. R. Doc. 51-3188; Filed, Mar. 12, 1951; 8:45 a. m.]

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[File No. 70-2464]

NEW ENGLAND GAS & ELECTRIC ASSN. AND NEW HAMPSHIRE ELECTRIC CO.

ORDER GRANTING AND PERMITTING APPLICATION-DECLARATION TO BECOME EFFECTIVE

At a regular session of the Securities and Exchange Commission, held at its office in the city of Washington, D. C., on the 6th day of March A. D. 1951.

New England Gas & Electric Association ("Negea"), a registered holding company, and its public utility subsidiary, New Hampshire Electric Company ("New Hampshire"), having filed a joint application-declaration regarding the surrender by Negea to New Hampshire of all the common stock of New Hampshire in exchange for 14,000 shares of $4.50 preferred stock and 150,000 shares of common stock and the sale of the preferred stock to underwriters

and the underwritten offer of sale of the common stock to its stockholders, both pursuant to the competitive bidding requirements of Rule U-50, and the donation by Negea to New Hampshire of all the common stock of Kittery Electric Light Company ("Kittery"); and

New Hampshire having applied for an order pursuant to section 3 (a) (2) exempting it from the provisions of the act upon acquisition of all the common stock of Kittery; and

Public hearings having been held after appropriate notice, and the Commission having considered the record and filed its findings and opinion herein:

*It is ordered,* That said application-declaration be, and the same hereby is, granted and permitted to become effective forthwith, subject, however, to the terms and conditions prescribed in Rule U-24 and to the further condition that the proposed issuance and sale by New Hampshire of the preferred and common stocks of New Hampshire shall not be consummated until the results of competitive bidding, pursuant to Rule U-50, have been made a matter of record herein and a further order shall be entered with respect thereto, which order shall contain such further terms and conditions as may then be deemed appropriate, for which purpose jurisdiction be, and the same, hereby is, reserved.

*It is further ordered,* That jurisdiction be, and the same hereby is, reserved over all fees and expenses to be incurred in connection with the proposed transactions.

*It is further ordered,* Pursuant to section 3 (a) (2) of the act, that New Hampshire, upon acquisition of the common stock of Kittery, be, and the same hereby is, exempted as a holding company from all the provisions of the act.

By the Commission.

[SEAL] ORVAL L. DUBOIS,
*Secretary.*

[F. R. Doc. 51-3189; Filed, Mar. 12, 1951; 8:45 a. m.]

## DEPARTMENT OF JUSTICE

### Office of Alien Property

AUTHORITY: 40 Stat. 411, 55 Stat. 839, Pub. Laws 322, 671, 79th Cong., 60 Stat. 50, 925; 50 U. S. C. and Supp. App. 1, 616; E. O. 9193, July 6, 1942, 3 CFR, Cum. Supp., E. O. 9567, June 8, 1945, 3 CFR, 1945 Supp., E. O. 9788, Oct. 14, 1946, 11 F. R. 11981.

[Vesting Order 17452]

DR. HERZFELD-WUESTHOFF

In re: Debts owing to Dr. Herzfeld-Wuesthoff, also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff. F-28-22130; C-2, C-3.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That Dr. Herzfeld-Wuesthoff, also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff, whose last known address is Unter der Linden 21, Berlin W8, Germany, is a resident of Germany and a national of a designated enemy country (Germany);

2. That the property described as follows:

a. That certain debt or other obligation owing to Dr. Herzfeld-Wuesthoff, also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff, by Behr-Manning Corporation, Troy, New York, arising out of an account resulting from legal services rendered to said Behr-Manning Corporation, together with any and all accruals thereto, and any and all rights to demand, enforce and collect the same,

b. That certain debt or other obligation owing to Dr. Herzfeld-Wuesthoff, also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff, by Whittemore, Hulbert & Belknap, 3053 Penobscot Building, Detroit 16, Michigan, arising out of an account resulting from legal services rendered to said Whittemore, Hulbert & Belknap, together with any and all accruals thereto, and any and all rights to demand, enforce and collect the same,

c. That certain debt or other obligation owing to Dr. Herzfeld-Wuesthoff also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff, by Pierce & Scheffler, 1319 F Street NW., Washington 4, D. C., arising out of a credit balance resulting from legal services rendered to said Pierce & Scheffler, together with any and all accruals thereto, and any and all rights to demand, enforce and collect the same, and

d. That certain debt or other obligation owing to Dr. Herzfeld-Wuesthoff also known as Dr. Ing. Frank Herzfeld-Wuesthoff, as Dr. Ing. F. Herzfeld-Wuesthoff and as Dr. F. Wuesthoff, by Haseltine, Lake & Co., 19 West 44th Street, New York 18, New York, arising out of an account resulting from legal services rendered to said Haseltine, Lake & Co., together with any and all accruals thereto, and any and all rights to demand, enforce and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of, or on account of, or owing to, or which is evidence of ownership or control by, the aforesaid national of a designated enemy country (Germany);

and it is hereby determined:

3. That to the extent that the person named in subparagraph 1 hereof is not within a designated enemy country, the national interest of the United States requires that such person be treated as a national of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 26, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3175; Filed, Mar. 9, 1951; 8:55 a. m.]

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[Vesting Order 17473]

CREDIT SUISSE

In re: Accounts maintained in the name of Credit Suisse, Neuchatel, Switzerland, and owned by persons whose names are unknown. F-63-60 (Neuchatel).

Under the authority of the Trading With the Enemy Act, as amended, Executive Orders 9193, as amended, 9788 and 9989, and pursuant to law, after investigation, it is hereby found:

1. That the property described as follows: All property, rights and interests in the accounts identified in Exhibit A attached hereto and by reference made a part hereof, together with

(a) Any other property, rights and interests which represent accumulations or accruals to, changes in form of, or substitutions for, any of the property, rights and interests in said identified accounts on October 2, 1950, and which are now held in other accounts being maintained as blocked or otherwise subject to the restrictions of Executive Order 8389, as amended, or regulations, rulings, orders or instructions issued thereunder, and

(b) Any and all rights in, to and under any securities (including, without limitation, bonds, coupons, mortgage participation certificates, shares of stock, scrip and warrants) and any and all declared and unpaid dividends on any shares of stock in any of said accounts,

excepting from the foregoing, however, all lawful liens and setoffs of the respective institutions in the United States with whom the aforesaid accounts are maintained,

is property within the United States;

2. That the property described in subparagraph 1 hereof is owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or is evidence of ownership or control by persons, names unknown, who, if individuals, there is reasonable cause to believe are residents of a designated enemy country and which, if partnerships, associations, corporations, or other organizations, there is reasonable cause to believe are organized under the laws of a designated enemy country or on or since the effective date of Executive Order 8389, as amended, have had their principal places of business in a designated enemy country;

3. That the persons referred to in subparagraph 2 hereof are nationals of a designated enemy country;

and it is hereby determined:

4. That to the extent that the persons referred to in subparagraph 2 hereof are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country.

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended, and the term "designated enemy country" has reference to Germany or Japan.

Executed at Washington, D. C., on February 28, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

EXHIBIT A

| Column I | Column II |
|---|---|
| Name and address of institution which maintains account. | Designation of account |
| Credit Suisse, New York Agency, 30 Pine St., New York 5, N. Y. | a. Current account; b. General ruling No. 6 account, and c. Miscellaneous portfolio of stocks; as described by Credit Suisse, New York Agency, in its report on form OAP-700, bearing its serial No. 25. |

[F. R. Doc. 51-3179; Filed, Mar. 9, 1951; 8:56 a. m.]

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[Vesting Order 17446]

ANNA ELISABETH OTTO-SARAUW

In re: Bonds and bank account owned by Anna Elisabeth Otto-Sarauw. F-28-31117-A-1.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That Anna Elisabeth Otto-Sarauw, who on or since the effective date of Executive Order 8399, as amended, and on or, since December 11, 1941, has been a resident of Germany, is a national of a designated enemy country (Germany):

2. That the property described as follows:

a. One (1) New York Central Railroad Co., Refunding and Improvement 4½ Percent, Series A. Mortgage Bearer Bond, of $1,000 face value, bearing the number 40764, presently in the custody of Brown Brothers Harriman & Co., 59 Wall Street, New York 5, New York, in an account entitled "Banque Cantonale de Zurich, Zurich, Clients Account Blocked Account," together with any and all rights thereunder and thereto,

b. Two (2) Southern Pacific Co., (Oregon Lines) First Mortgage 4½ Percent Series A Bearer Bonds of $1,000 face value each, bearing the numbers 19358 and 38949, presently in the custody of Brown Brothers Harriman & Co., 59 Wall Street, New York 5, New York, in an account entitled "Banque Cantonale de Zurich, Zurich, Clients Account Blocked Account," together with any and all rights thereunder and thereto,

c. One (1) Kingdom of Denmark 34 Year External Loan 4½ Percent Bearer Bond of $1,000 face value, bearing the number M49476, presently in the custody of Brown Brothers Harriman and Co., 59 Wall Street, New York 5, New York, in an account entitled "Banque Cantonale de Zurich, Zurich, Clients Account Blocked Account," together with any and all rights thereunder and thereto,

d. One (1) Kingdom of Denmark 30 Year External Loan 5½ Percent Bearer Bond of $1,000 face value, bearing the number M22058, presently in the custody of Brown Brothers Harriman & Co., 59 Wall Street, New York 5, New York, in an account entitled "Banque Cantonale de Zurich, Zurich, Clients Account, Blocked Account," together with any and all rights thereunder and thereto, and

e. That certain debt or other obligation of Brown Brothers Harriman & Co., 59 Wall Street, New York 5, New York, in the amount of $389 as of January 19, 1951, held in an account entitled "Banque Cantonale de Zurich, Zurich, Clients Account, General Ruling No. 6 Account," maintained with the aforesaid company, and any and all rights to demand, enforce and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by, Anna Elisabeth Otto-Sarauw, the aforesaid national of a designated enemy country (Germany);

and it is hereby determined:

3. That to the extent that the person named in subparagraph 1 hereof is not within a designated enemy country, the national interest of the United States requires that such person be treated as a national of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 26, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3171; Filed, Mar. 9, 1951; 8:54 a. m.]

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[Vesting Order 17441]

JAPANESE CHINAWARE AND NOVELTY IMPORTERS' ASSN. OF NEW YORK

In re: Bank account owned by Japanese Chinaware and Novelty Importers' Association of New York. D-39-292.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation:

1. It is hereby found that Morimura Bros., Inc., the last known address of which is Japan, is a corporation, partnership, association, or other business organization, organized under the laws of Japan and which has or, since the effective date of Executive Order 8389, as amended, has had its principal place of business in Japan and is a national of a designated enemy country (Japan);

2. It having been found and determined under the vesting orders, the numbers and dates of which are set forth below, that the following named companies are nationals of a designated enemy country (Japan);

| Name | Vesting order | Date |
|---|---|---|
| Haruta & Co., Inc. | 173 | Sept. 8, 1942 |
| Mogi, Mamonoi & Co. | 92 | Aug. 6, 1942 |
| Nagoya Seito Kaisha, Ltd. | 176 | Sept. 28, 1942 |
| | 379 | Nov. 18, 1942 |
| Taiyo Trading Co., Inc. | 147 | Sept. 17, 1942 |
| | 387 | Nov. 19, 1942 |

3. It is hereby found that Japanese Chinaware and Novelty Importers' Association of New York is a voluntary unincorporated association, whose principal place of business is in New York, New York, and is or, since the effective date of Executive Order 8389, as amended, has been controlled, directly or indirectly by the aforesaid Haruta and Company, Inc., Morimura Bros., Inc., Mogi, Mamonoi & Company, Nagoya Saito Kaisha, Ltd., and Taiyo Trading Company, Inc., and is a national of a designated enemy country (Japan);

4. It is hereby found that the property described as follows: That certain debt or other obligation owing to Japanese Chinaware and Novelty Importers' Association of New York, by Central Hanover Bank and Trust Company, 70 Broadway, New York, New York, arising out of a checking account, entitled Japanese Chinaware and Novelty Importers' Association of New York, maintained at the aforesaid company, and any and all rights to demand, enforce and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by, Japanese Chinaware and Novelty Importers' Association of New York, the aforesaid national of a designated enemy country (Japan);

and it is hereby determined:

5. That Japanese Chinaware and Novelty Importers' Association of New York is controlled by, or acting for or on behalf of, a designated enemy country (Japan), or persons within such country, and is a national of a designated enemy country (Japan); and

6. That to the extent that the persons named in subparagraphs 1, 2 and 3 hereof are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country (Japan).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 26, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3169; Filed, Mar. 9, 1951; 8:54 a. m.]

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[Vesting Order 17383]

CHARLOTTE SCHEPELMANN

In re: Stock owned by Charlotte Schepelmann. F-28-31225.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That Charlotte Schepelmann, whose last known address is Germany, is a resident of Germany and a national of a designated enemy country (Germany);

2. That the property described as follows:

a. Twenty-five (25) shares of $1.00 par value common capital stock of New Mexico Gold Producers Corporation, evidenced by a certificate numbered 531, registered in the name of Charlotte Schepelmann, and presently in the custody of the Department of State, Division of Protective Services, 515 Twenty-second Street NW., Washington, D. C., together with all declared and unpaid dividends thereon,

b. Two (2) shares of $20.00 par value common capital stock of American Commercial Alcohol Corporation, evidenced by a certificate numbered CO10257, registered in the name of Miss Charlotte Schepelmann, and presently in the custody of the Department of State, Division of Protective Services, 515 Twenty-second Street NW., Washington, D. C., together with all declared and unpaid dividends thereon, and

c. One (1) Scrip Certificate for four-fifths (4/5) share of $20.00 par value common capital stock of American Distilling Company, 247 Park Avenue, New York, New York, said certificate numbered SC680 and presently in the custody of the Department of State, Division of Protective Services, 515 Twenty-second Street NW., Washington, D. C., and any and all rights thereunder and thereto,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of, or on account of, or owing to, or which is evidence of ownership or control by, the aforesaid national of a designated enemy country (Germany);

and it is hereby determined:

3. That to the extent that the person named in subparagraph 1 hereof is not within a designated enemy country, the national interest of the United States requires that such person be treated as a national of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 13, 1951.

For the Attorney General.

[SEAL] PAUL V. MYRON,
*Deputy Director,*
*Office of Alien Property.*

[F. R. Doc. 51-3219; Filed, Mar. 12, 1951; 8:52 a. m.]

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[Vesting Order 17430]

INDUSTRIAL BANK OF JAPAN, LTD.

In re: Bonds owned by the Industrial Bank of Japan, Ltd. F-39-132-A-1/2.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That the Industrial Bank of Japan, Ltd., the last known address of which is Tokyo, Japan, is a corporation, partnership, association or other business organization, organized under the laws of Japan, and which has or since the effective date of Executive Order 8389, as amended, has had its principal place of business in Japan and is a national of a designated enemy country (Japan);

2. That the property described as follows:

a. Twenty-two (22) Russian Imperial Government six and one-half percent (6½ percent) bonds, due June 18, 1919, of Twenty-five Thousand Dollar ($25,000.00) face value each, bearing the numbers D888/909, both inclusive, registered in the name of The Industrial Bank of Japan, Ltd., Tokyo, Japan, presently in the custody of The Guaranty Trust Company of New York, 140 Broadway, New York 15, New York, together with any and all rights thereunder and thereto, and

b. Fifty (50) Russian Imperial Government six and one-half percent (6½ percent) bonds, due June 18, 1919, of Ten Thousand Dollar ($10,000.00) face value each, registered in the name of William Mehte (nominee) and bearing the numbers C18/67, both inclusive, presently in the custody of The National City Bank, together with any and all rights thereunder and thereto,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of, or on account of, or owing to, or which is evidence of ownership or control by, the aforesaid national of a designated enemy country (Japan);

and it is hereby determined:

3. That to the extent that the person named in subparagraph 1 hereof is not within a designated enemy country, the national interest of the United States requires that such person be treated as a national of a designated enemy country (Japan).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 21, 1951.

For the Attorney General.

[SEAL] PAUL V. MYRON,
*Deputy Director,*
*Office of Alien Property.*

[F. R. Doc. 51-3221; Filed, Mar. 12, 1951; 8:52 a. m.]

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[Vesting Order 17475]

HELEN KURZ ET AL.

In re: Rights of Helen Kurz et al., under insurance contracts. File Nos. F-28-28976-H-2, H-3.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Ex-

ecutive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That Helen Kurz, whose last known address is Germany, is a resident of Germany and a national of a designated enemy country (Germany);

2. That the domiciliary personal representatives, heirs, next of kin, legatees and distributees, names unknown, of Helen Kurz, who there is reasonable cause to believe are residents of Germany, are nationals of a designated enemy country (Germany);

3. That the net proceeds due or to become due under contracts of insurance evidenced by policies numbered 66967565 and 84740865, issued by The Prudential Insurance Company of America, Newark, New Jersey, to Helen Kurz, and any and all other benefits and rights of any kind or character whatsoever under or arising out of said contracts of insurance except those of the aforesaid The Prudential Insurance Company of America, together with the right to demand, enforce, receive and collect the same is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by Helen Kurz or the domiciliary personal representatives, heirs, next of kin, legatees and distributees, names unknown, of Helen Kurz, the aforesaid nationals of a designated enemy country (Germany);

and it is hereby determined:

4. That to the extent that the person named in subparagraph 1 hereof, and the domiciliary personal representatives, heirs, next of kin, legatees and distributees, names unknown, of Helen Kurz, are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on March 1, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3222; Filed, Mar. 12, 1951; 8:53 a. m.]

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[Vesting Order 17486]

JAPAN

In re: Debt owing to Japan. F-39-4691-E-1.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

That the property described as follows: That certain debt or other obligation of The Northern Trust Company, 50 South LaSalle Street, Chicago 90, Illinois, in the amount of $10,043.00 as of December 31, 1945, representing a portion of a checking account entitled Kahachiro Omori, maintained at the aforesaid bank, and any and all rights to demand, enforce and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by, a designated enemy country (Japan).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The term "designated enemy country" as used herein shall have the meaning prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on March 2, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3224; Filed, Mar. 12, 1951; 8:53 a. m.]

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[Vesting Order 17393]

AMALIE STOCKMANN ET AL.

In re: Stocks and bank account owned by Amalie Stockmann, Heinrich Borchers and Agnes Borchers. D-28-12969.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That Amalie Stockmann, Heinrich Borchers and Agnes Borchers, whose last known addresses is Junkerstrasse 34, Oldenburg i/Oldenburg, Germany, are residents of Germany and nationals of a designated enemy country (Germany);

2. That the property described as follows:

a. Six and one-half (6½) shares of preferred stock of Pacific Steamship Lines, Lt., San Francisco, California, a corporation organized under the laws of the State of California, evidenced by certificate numbered P 703, in the name of Haydn P. Phennah, and endorsed by him in blank, and presently in the custody of H. Otto Giese, Hoge Building, Seattle, Washington, together with all declared and unpaid dividends thereon,

b. Twenty (20) shares Class A common stock of Pacific Steamship Lines, Ltd., San Francisco, California, a corporation organized under the laws of the State of California, evidenced by certificate numbered A 1535, in the name of Haydn P. Phennah, and endorsed by him in blank, and presently in the custody of H. Otto Giese, Hoge Building, Seattle, Washington, together with all declared and unpaid dividends thereon, and

c. That certain debt or other obligation of Seattle Trust and Savings Bank, Seattle, Washington, arising out of Blocked Account numbered 3282, designated "Estate of Louis S. Borchers, Deceased, by H. Otto Giese, Trustee," maintained at the aforesaid bank, and any and all rights to demand, enforce and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by, Amalie Stockmann, Heinrich Borchers and Agnes Borchers, the aforesaid nationals of a designated enemy country (Germany);

and it is hereby determined:

3. That to the extent that the persons named in subparagraph 1 hereof are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on February 15, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3220; Filed, Mar. 12, 1951; 8:52 a. m.]

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[Vesting Order 17485]

GERMAN NATIONALS

In re: Debt owing to German nationals whose names are unknown. D-28-12526-E-1.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

1. That the property described in subparagraph 4 hereof was received by Upright Associates, 45 East 17th Street, New York, New York, for deposit in a safekeeping account at Manufacturers Trust Company, 221 4th Avenue, New York 4, New York, under the designation

Upright Associates Special Blocked Account;

2. That although the names of the owners of the property described in subparagraph 4 hereof are not available, such persons are within Germany;

3. That the owners of the property described in subparagraph 4 hereof who there is reasonable cause to believe are residents of Germany are nationals of a designated enemy country (Germany);

4. That the property described as follows: That certain debt or other obligation of Upright Associates, 45 East 17th Street, New York, New York, in the amount of $3,108.69, representing funds collected by said Upright Associates for and on behalf of the persons identified in subparagraph 3 hereof, deposited in an account with Manufacturers Trust Company, 221 Fourth Avenue, New York 4, New York, entitled Upright Associates Special Blocked Account, and thereafter withdrawn from said account by said Upright Associates, together with any and all accruals thereto and any and all rights to demand, enforce, and collect the same,

is property within the United States owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by the persons referred to in subparagraph 3 hereof, the aforesaid nationals of a designated enemy country (Germany);

and it is hereby determined:

5. That to the extent that the persons referred to in subparagraph 3 hereof are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on March 2, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3223; Filed, Mar. 12, 1951; 8:53 a. m.]

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[Return Order 870]

KONINKLIJKE INDUSTRIEELE MAATSCHAPPIJ VOORHEEN NOURY AND VAN DER LANDE N. V.

Having considered the claim set forth below and having issued a determination allowing the claim, which is incorporated by reference herein and filed herewith,

*It is ordered,* That the claimed property, described below and in the determination, including all royalties accrued thereunder and all damages and profits recoverable for past infringement thereof, be returned after adequate provision for taxes and conservatory expenses:

*Claimant, Claim No., Notice of Intention To Return Published, and Property*

Koninklijke Industrieele Maatschappij Voorheen Noury & Van der Lande N. V., Deventer, The Netherlands; Claim No. 6531; December 28, 1950 (15 F. R. 9368); property described in the following Vesting Orders: No. 291 (7 F. R. 9334, November 26, 1942); No. 671 (8 F. R. 5004, April 17, 1943); No. 1825 (8 F. R. 10911, August 5, 1943) relating to United States Letters Patent and United States Patent Applications identified in Schedule A, attached hereto and made a part hereof. This return shall not be deemed to include the rights of any licensees under the above patent or patent applications.

Appropriate documents and papers effectuating this order will issue.

Executed at Washington, D. C., on March 7, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

SCHEDULE A—PATENTS ASSIGNED TO KONINKLIJKE INDUSTRIEELE MAATSCHAPPIJ VOORHEEN NOURY & VAN DER LANDE N. V.

[Vested by Vesting Order No. 671]

| Patent No. | Date issued | Inventor | Title | Assigned |
|---|---|---|---|---|
| 2,043,940 | 6- 9-36 | E. Van Thiel | Apparatus for the Manufacture of Yeast | 5- 2-36 |
| 2,081,097 | 5-18-37 | W. Reinders | Manufacture of Hydrogen Peroxide | 3-28-36 |
| 2,105,438 | 1-11-38 | H. Hartman | Process and Apparatus for Producing Percompounds. | 6-18-35 |
| 2,117,255 | 8- 8-39 | R. Priester | Resins and Process of Making Same | 3-13-36 |
| 2,118,903 | 5-31-38 | E. Staudt | Process for the Manufacture of Nitrogen Trichloride. | 6-28-38 |
| 2,118,904 | 5-31-38 | E. Staudt, G. Van der Lee | Process for the Manufacture of Chloro Amines | 6-29-38<br>7-12-38 |
| 2,119,188 | 5-31-38 | B. L. M. Van der Lande, E. Van Thiel. | Process for Aerating Liquids in the Production of Yeast. | 12-16-35 |
| 2,128,732 | 8-30-38 | R. Priester | Process for Manufacturing Driers | 10- 5-35 |
| 2,155,914 | 4-25-39 | G. Van der Lee | Process for the Preparation of a Bleaching and Sterilizing Agent. | 2- 9-37 |
| 2,163,898 | 6-27-39 | J. A. L. Van der Lande | Process for the Production of Hydrogen Peroxide | 7-21-37 |
| 2,185,967 | 1- 2-40 | R. Priester | Linoxin Like Material and Process of Manufacture. | 8-17-37 |
| 2,195,225 | 3-26-40 | do | Process for the Manufacture of Drying Oil from Castor Oil. | 11-15-38 |
| 2,199,942 | 5- 7-40 | E. Staudt | Process for Producing Nitrogen Trichloride | 6-12-37 |
| 2,226,830 | 12-31-40 | R. Priester | Process for the Manufacture of Drying Oils | 12-15-37 |
| 2,226,831 | 12-31-40 | do | do | 12-15-37 |
| 2,228,154 | 1- 7-41 | do | Drying Oil and Process of Making Same | 6-10-38 |
| 2,248,650 | 7- 8-41 | G. Van der Lee | Process for Producing Nitrogen Trichloride | 2- 9-37 |
| 2,280,082 | 4-21-42 | R. Priester | Manufacture of Drying Oils | 6- 2-39 |

PATENT APPLICATIONS ASSIGNED TO KONINKLIJKE INDUSTRIEELE MAATSCHAPPIJ VOORHEEN NOURY & VAN DER LANDE N. V.

[Vested by Vesting Order No. 291]

| Serial No. | Date filed | Inventor | Title | Assigned |
|---|---|---|---|---|
| 164,989 (now Pat. No. 2,300,439). | 9-21-37<br>[1](11- 3-42) | G. Van der Lee | Stable Mixtures Containing Levoascorbic Acid or the Like. | 9- 9-37 |
| 810,261 (now Pat. No. 2,351,970). | 12-20-39<br>[1](6-20-44) | M. P. J. M. Jansen | Process for the Separation of Yeast from Yeast Suspensions. | 11-25-39 |
| 362,682 (now Pat. No. 2,309,273). | 10-24-40<br>[1](1-26-43) | R. Priester | Making Drying Oils | 10- 2-40 |
| 386,748 (now Pat. No. 2,344,429). | 4- 3-41<br>[1](3-14-44) | D. W. van Gelder | Process of Purifying Sulphuric Acid Solutions. | 3- 4-41 |
| 413,022 (now Pat. No. 2,356,632). | 9-30-41<br>[1](8-22-44) | B. J. Van den Dool | Pill Box | 5-23-41 |

[Vested by Vesting Order No. 1825]

| | | | | |
|---|---|---|---|---|
| 320,517 | 2-23-40 | C. S. Neuberg | Process for the Production of Saccharic Acid. | 2- 3-40 |

[1] The date in parenthesis refers to the date of issuance of the patent.

[F. R. Doc. 51-3227; Filed, Mar. 12, 1951; 8:54 a. m.]

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[Vesting Order 16424, Amdt.]

MRS. HERMANN ROESING ET AL.

In re: Rights of Mrs. Hermann Roesing et al., under insurance contracts. File Nos. F-28-30641 H-1, H-2.

Under the authority of the Trading With the Enemy Act, as amended, Executive Order 9193, as amended, and Executive Order 9788, and pursuant to law, after investigation, it is hereby found:

Vesting Order 16424 dated December 13, 1950, is hereby amended to read as follows:

1. That Mrs. Hermann Roesing, also known as Gabriele Paula Roesing, Marlo Helm, Hermann Max Fritz Roesing, Gerd Udo Ellerbroek, Antje Kathrin Ellerbroek and Mrs. George (Georg) Hirschfeld, also known as Ada Hirschfeld, whose last known address is Germany, are residents of Germany and nationals

of a designated enemy country (Germany);

2. That the net proceeds due or to become due under contracts of insurance evidenced by policies numbered 122552 and 124607, issued by The Equitable Life Assurance Society of the United States, New York, New York, to Phillip H. N. Wustendorfer, together with the right to demand, receive and collect said net proceeds,

is property within the United States, owned or controlled by, payable or deliverable to, held on behalf of or on account of, or owing to, or which is evidence of ownership or control by, the aforesaid nationals of a designated enemy country (Germany);

and it is hereby determined:

3. That to the extent that the persons named in subparagraph 1 hereof are not within a designated enemy country, the national interest of the United States requires that such persons be treated as nationals of a designated enemy country (Germany).

All determinations and all action required by law, including appropriate consultation and certification, having been made and taken, and, it being deemed necessary in the national interest,

There is hereby vested in the Attorney General of the United States the property described above, to be held, used, administered, liquidated, sold, or otherwise dealt with in the interest of and for the benefit of the United States.

The terms "national" and "designated enemy country" as used herein shall have the meanings prescribed in section 10 of Executive Order 9193, as amended.

Executed at Washington, D. C., on March 1, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3225; Filed, Mar. 12, 1951; 8:53 a. m.]

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[Return Order 850]

ENRICO PHILIPPI

Having considered the claim set forth below and having issued a determination allowing the claim, which is incorporated by reference herein and filed herewith,

*It is ordered,* That the claimed property, described below and in the determination, be returned, subject to any increase or decrease resulting from the administration thereof prior to return, and after adequate provision for taxes and conservatory expenses:

*Claimant, Claim No., Notice of Intention To Return Published, and Property*

Enrico Philippi, New York, N. Y.; Claim No. 4392; September 30, 1950 (15 F. R. 6622); $1,870.87 in the Treasury of the United States.

Appropriate documents and papers effectuating this order will issue.

Executed at Washington, D. C., on March 6, 1951.

For the Attorney General.

HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3226; Filed, Mar. 12, 1951; 8:54 a. m.]

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[Return order 871]

N. V. NOURY & VAN DER LANDE'S EXPLOITATIEMAATSCHAPPIJ

Having considered the claim set forth below and having issued a determination allowing the claim, which is incorporated by reference herein and filed herewith,

*It is ordered,* That the claimed property, described below and in the determination, including all royalties accrued thereunder and all damages and profits recoverable for past infringement thereof, be returned after adequate provision for taxes and conservatory expenses:

*Claimant, Claim No., Notice of Intention To Return Published, and Property*

N. V. Noury & Van der Lande's Exploitatiemaatschappij, Deventer, The Netherlands; Claim No. 6532; Dec. 22, 1950 (15 F. R. 9216); property described in Vesting Order No. 671 (8 F. R. 5004, April 17, 1943) relating to United States Letters Patent Nos. 1,866,412; 2,149,682 and 2,156,737. Property described in Vesting Order No. 1550 (8 F. R. 8564, June 22, 1943) as Transaction Control No. 312, relating to a disclosure of invention entitled "Improvement of the Baking Strength of Flour", inventor Hanns John. This return shall not be deemed to include the rights of any licensees under the above patents, or disclosure of invention.

Appropriate documents and papers effectuating this order will issue.

Executed at Washington, D. C., on March 7, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3228; Filed, Mar. 12, 1951; 8:54 a. m.]

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[Return Order 896]

PAUL GARNIER

Having considered the claim set forth below and having issued a determination allowing the claim, which is incorporated by reference herein and filed herewith,

*It is ordered,* That the claimed property, described below and in the determination, including all royalties accrued thereunder and all damages and profits recoverable for past infringement thereof, be returned after adequate provision for taxes and conservatory expenses:

*Claimant, Claim Number, Notice of Intention To Return Published, and Property*

Paul Garnier, Lyon, France; Claim No. 29556; January 23, 1951 (16 F. R. 636); property described in Vesting Order No. 1028 (8 F. R. 4205, April 2, 1943) relating to United States Patent Application Serial No. 451,094. This return shall not be deemed to include the rights of any licensees under the above patent application.

Appropriate documents and papers effectuating this order will issue.

Executed at Washington, D. C., on March 7, 1951.

For the Attorney General.

[SEAL] HAROLD I. BAYNTON,
*Assistant Attorney General,*
*Director, Office of Alien Property.*

[F. R. Doc. 51-3229; Filed, Mar. 12, 1951; 8:55 a. m.]